THE SYSTEM OF NATIONAL FINANCE

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BY E. HILTON YOUNG

SECOND EDITION

BY E. HILTON YOUNG AND N. E. YOUNG

"*Mr. Micawber conjured me to observe that if a man had twenty pounds a year for his income and spent nineteen pounds nineteen shillings and sixpence he would be happy, but that if he spent twenty pounds one, he would be miserable. After which he borrowed a shilling of me for porter and cheered up.*"—DAVID COPPERFIELD.



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# PREFACE TO SECOND EDITION

THE Public having been kind enough to ask for a second helping of this book, with the help of Mr. N. E. Young of the Treasury I have shortened it, revised it, and brought it up to date. In doing so I have been surprised to find how few changes the war has made in our financial system. The chapters on debt had to be rewritten; but not, as I expected, the rest of the book. Very sensibly, we put our ordinary financial machine away in the cupboard at the beginning of the war, and financed the war by special machinery. The ordinary machine thus escaped unfair wear and tear; and at the end of the war we were able to take it out and bring it into use again, as good as new, and but little changed.

The chief purpose of the book remains, as in the first edition, to explain and not to criticise, and to explain machinery, not policy.

E. H. Y.

*April*, 1924.

# PREFACE TO FIRST EDITION

BITTER and unavailing are the regrets of a reader who has read through a book, and wakes on the last page to the discovery that it is all about something other than he supposed. To save an intending reader from that disappointment, it will be as well to set down here what this book is not about. It is not about public finance in the abstract; that ground is well covered by Professor Bastable's "Public Finance," and other works on the same subject. It is not a history of British public finance in modern times. We are now fortunate enough to have that story admirably told in three books, Lord Iddesleigh's "Twenty Years of Financial Policy" (1842–62), Lord Buxton's "Finance and Politics" (1862–87), and Mr. Bernard Mallet's "British Budgets" (1887–1913), which taken together provide us with a detailed record of the subject and a commentary upon its developments during the last seventy years. It is not a history of taxation: for that we have Stephen Dowell's big work. Nor does it seek to be a compendious work of reference in which may be found all the laws, rules, principles, authorities, and precedents relating to the nation's financial business. That has yet to be compiled.

Its ambition is to be a primer of the system on

which the financial business of the nation is conducted at the present time. It is intended as a first aid to those who need to understand something about the manner in which the nation gets and spends its revenue, borrows money, and keeps its accounts. With that end before it, it avoids history, and does without figures as far as possible.

Much that is not readily intelligible in our financial system is made clear by a word of explanation from those actually engaged in working it; and for explanations of the sort most kindly and helpfully given, I am in debt to many creditors. My thanks are specially due to Mr. F. D. Acland, M.P., formerly Financial Secretary of the War Office, and now Parliamentary Under-Secretary of the Foreign Office; Sir Charles Harris, K.C.B., Assistant Financial Secretary of the War Office; Mr. F. W. A. Clarke, Accountant and Comptroller General of the Board of Customs and Excise; Mr. W. G. Turpin, Comptroller General of the National Debt Office; Mr. C. L. Davies, Assistant Paymaster General; Mr. V. W. Baddeley, C.B., Assistant Secretary to the Admiralty for Financial Duties; Mr. H. V. Reade, C.B., Principal of the Statistical Office at the Board of Customs and Excise; and Mr. F. W. Bartlett, Principal Clerk in the Pay Office. To the Officials of the Bank of England I owe a debt in this respect that grows daily.

What I have learnt from these is as much as it is good for a taxpayer to know and no more; and the explanations which I have received, given with the unfailing courtesy of the Civil Service, would, no doubt, have been equally at the disposal of anybody else who was concerned to inquire into these matters. But that does not affect the warmth of

my gratitude. Needless to say, none of those to whom I here render my thanks is in any way responsible for any statement of fact made in this book, still less for any expression of opinion.

E. H. Y.

*January*, 1915.

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REVENUE AND EXPENDITURE

# CHAPTER I

## PRELIMINARIES

ALL other particulars of good government profit a state little unless its system of public finance is well designed, well understood, and well protected and maintained. The last two needs depend much upon the second. Unless the system is well understood by an instructed public, and the financial administration is constantly illuminated by the light of public opinion, there is danger both that its methods may lapse into mere routine and inefficiency, and that the administrators may be tempted to take liberties. It is the financial engine that drives the state along, and it is public opinion and public criticism that keep the engine working smoothly and at full power. Unfortunately criticism by the light of nature alone is of little use. The critic needs some acquaintance with the way in which the nation manages its money and keeps its accounts; but a little goes a long way. So much as may be gained from the following pages should go far enough at least to enable a critic to confront questions of financial policy without undue dismay.

### SOME GENERAL PRINCIPLES

The financial business of a state is not much different in nature from that of a private person.

A state has to live and to do its work, and for that it must have money. Its money must be got from somewhere; it must be kept somewhere while the state has got it; and it must be paid to somebody in return for goods and services. The chief difference between the state and a man in this connection is that, whereas a man gets as much money as he can, sure to find a use for all that he can get, the state gets (or at least ought to get) only so much money as it needs for certain specific uses prescribed beforehand. The uses may change from year to year, and in these days of legislative activity they have a tendency constantly to increase; but they have always their definite limits. Otherwise the financial affairs of both the state and the individual have the same chief divisions, three in number, getting, keeping, and spending.

The state gets its money in three ways: as taxes which it levies; as fees for services which it performs, in the law courts for instance; and as prices for goods which it sells. Keeping the state's money is a simple matter. It is kept as that of the individual is kept. Just as a householder keeps a little ready money in his pocket, as little as possible, for safety's sake, and leaves the rest at his bank; so the state keeps small cash balances, as small as possible, in the pockets of the servants to whom it entrusts the duty of making payments for it, and leaves the rest at the Bank of England. In the matter of payment too the state's household bills are very like those of the father of a British family. There are payments which may be classed as establishment charges, the wages of servants, civil, military, and naval, and the upkeep of buildings. There are bills for goods bought, of which the biggest are for ships and guns and

munitions of war: these may be compared with the householder's burglary and fire insurance premiums. There is interest to be paid on the national debt. "Effective" charges is the technical name given to all these. In addition the state has pensions to pay to its servants who have earned their ease personally, and to some lucky few who have earned it by the exertions of their ancestors, charges which are called "non-effective."

So, as in the case of any one of us, in the case of the state also revenue and expenditure are the two words that sum up the whole of financial business. To trace the taxpayer's pound from its exit out of his pocket to its entry into the pocket of the state as revenue, and back again as expenditure into the pocket of some other taxpayer who is the state's creditor, is the work before us. It will simplify that work if now at the outset certain general principles are stated which govern the whole process.

In financial business as in all other functions of government the body of the state has two members, the legislative and the executive. The Legislature says what is to be done and the Executive does it. The functions of the state for the performance of which it needs money, are, as said, unlike those of the individual, strictly limited. The Legislature lays down what those functions are, how much money is to be spent on each, and how the funds needed are to be obtained. The Executive then proceeds to obtain them in the appointed manner and to apply them to the appointed ends. The sovereign legislative power is with Parliament, subject to the Crown's formal power of veto, now mummified. Part of the provision which Parliament makes as to how much money is to be spent and

what it is to be spent upon is made for a year only, and is made afresh every year. Part has been made at various times once for all. But every penny that is collected and every penny that is spent is collected and spent under the authority of some Act of Parliament, permanent or temporary. In the matter and manner of getting and spending the Executive is wholly subject to Parliament and has no power to move a hair's breadth beyond the powers which Parliament entrusts to it.

At the top of the Executive is the Crown; and by the Crown is meant in practice its constitutional ministers, responsible to Parliament. The true head therefore of the financial administration is the Cabinet. There sit the responsible ministers who are the heads of the administrative departments, so that from the collector of income-tax round the corner and from the paymaster sub-lieutenant on a warship at Hong Kong to the Prime Minister in Downing Street there is a direct chain of responsibility and control.

In its work of collecting the revenue and of spending it the official hierarchy is guided by several general principles, laid down at various times by Parliament. Underlying as they do the whole business of financial administration, they should be mentioned here at the earliest possible opportunity. It is all the more necessary because much of our more detailed inquiry into the system of national finance must be concerned with the manner in which, to meet the exigencies of practice, departures great and small are made from the strict application of the general principles.

(1) The first principle is that no money can be got and none spent save under the authority of

Parliament. An amplification of that is that no money got can be spent save for the purpose to which Parliament has appropriated it.

(2) The second is that all money got must be paid into a single fund, the Consolidated Fund, and that all money spent must be paid out of that fund. That is a great principle, but it is a difficult one to observe. In practice there are many minor exceptions to it.

(3) The third is that the unit of time in financial administration is the year. The financial year now begins on April 1st and ends on March 31st. Expenditure for the year must be met out of revenue for the year, and revenue must not be left to accumulate from year to year. That again is rather a pious aspiration than a rigid rule. But the greater the financial morality of an administration, the more strictly it adheres to it.

(1) Such rules as these need, and are capable of, as little apology as Euclid's postulates. In the first are implicit the longest chapters of our political history. Appropriation, as we shall see, is the check which Parliament imposes upon the power of the Executive, to keep it subservient to the sovereign power of the Legislature.

(2) The second rule, that about the Consolidated Fund, is the sheet anchor of simplicity and efficiency in the nation's accounts. It is of use also to Parliament as a way of maintaining its control over the whole of revenue and expenditure, because in the Consolidated Fund it has the public money in full view and under its thumb. For that reason it has been resolved by the House of Commons "that this House cannot be the effectual guardian of the Revenues of the State unless the whole amount of

the taxes and of various other sources of income received for the Public Account be either paid in or accounted for to the Exchequer." [1]

(3) That revenue and expenditure should balance year by year is the golden rule of economy. It is even an absolute essential of solvency. Bankruptcy is the port towards which a state steers that allows its debts to accumulate. To obscure the fact that they are being allowed to accumulate by raising loans to pay them off temporarily can only prolong the journey. The converse form of accumulation, the accumulation of a balance of revenue from year to year, is equally uneconomic. It needlessly deprives the nation of wealth for which profitable uses could be found, and keeps it lying idle and sterile.

These are elementary principles. They are buried so deep at the root of our subject that they are apt to be forgotten altogether. To dig them up and have a look at them just once before we go on is not waste of time if it fixes in our minds the idea that the purpose of all financial machinery is to secure in the first place full parliamentary control of incomings and outgoings; in the second place, that the one shall yearly balance the other; in the third, that the taxpayer shall not be asked to find more money than is needed; and lastly, most important, and most difficult of attainment, that there shall be no waste in expenditure.

### Organisation

In matters of government a system well designed is a very necessary thing; but in practice a system,

[1] Resolution of 30th May, 1848.

however well designed, is worth just as much as is due to the integrity, ability, and loyalty of the men that work it and no more. Ultimately the true safeguard for pure and efficient administration in financial matters is the high tradition of the public service, both in the Legislature and in government offices. No tightening of the screws of system could possibly compensate for a screw loose there. The public spirit of the servants of the state is the spirit that gives life to dead rules and regulations; and it is the confidence with which we have learnt to rely upon it in our own affairs that is our most valuable public asset. Men matter more than rules, and what matters most in the servants of the commonwealth is that they should have those personal qualities which we have learnt to count upon in our civil servants.

But of almost equal importance in its effect upon the working of a system is the manner in which men are organised to work it. A brief account therefore will be useful of the principal organs of government which deal with our financial affairs.

The triple Legislature of King, Lords, and Commons we may pass over with a reference, and turn to the Executive. At its head stands the Cabinet, the committee of ministers who are mostly heads of executive departments, over which presides the Prime Minister.

Immediately below these high powers stands the Treasury. The Treasury is a Government office which exercises general control over the whole business of financial administration. Its obscure and gloomy haunt at Treasury Chambers in Whitehall is the centre of the web. Nominally it is controlled by a board which holds a commission to

perform duties performed of old by the Lord High Treasurer. The Board of Lords Commissioners of the Treasury consists in theory of a First Lord, the Chancellor of the Exchequer, who is also Under-Treasurer, and four or five Junior Lords, with a parliamentary secretary and a financial secretary, all of whom are members of Parliament and of the Ministry. But in practice this Board does not act. The First Lordship and the Junior Lordships are purely political offices. The office of First Lord is usually held by the Prime Minister, and it is as First Lord that he draws a salary from public funds. To the junior lordships are appointed those who are to act as party "whips" in Parliament. The office of Parliamentary Secretary is also wholly political: to that is appointed the member of Parliament who is to act as Chief Whip. First and Junior Lords have nothing to do with the administrative work of the office, except that they are useful to sign documents. It is the Chancellor of the Exchequer who is the executive head of the department, with the Financial Secretary as his assistant in the work, both in Parliament and in the office. The Exchequer of which he is called Chancellor, as will be seen, has now no real existence. It is as head of the Treasury, which is the central financial department, that he is in substance the Minister of Finance.

The Treasury is a co-ordinating department in the organisation of the civil service. It is in communication with every other government office, and almost all its work consists of considering applications from other departments. Its permanent head is a Permanent Secretary, who is not merely the head of the department, but also the connecting link between the Cabinet and the Civil Service, of which

he is the head. The Treasury is divided into three departments, (1) Finance, (2) Supply Services, and (3) Establishments. Over each of these departments there is a Controller, who holds the threads of all general questions relating to his department, and directs the activities of the lesser units, the divisions. The work of the departments is generally :—

*Finance* :—revenue, loans, the administration of the public debt, the preparation of estimates and money bills, the consolidated fund, financial relations with the Dominions and Foreign Countries ; questions of banking, currency and the foreign exchanges, financial procedure, audit and the form of public accounts ;

*Supply Services* :—questions relating to public expenditure chargeable against moneys provided by Parliament ;

*Establishments* :—questions of personnel and remuneration, the organisation of all civilian posts and establishments whether in civil or military departments, and superannuation.

Each department of the Civil Service is in constant communication with one of the divisions of the Treasury as regards its work, and with another as regards the detailed staff needed to carry out that work.

Thus the Treasury is in touch with every other department ; but as the centre of financial administration it keeps certain departments, the work of which is principally financial, especially close under its wing. Directly correlated to the Treasury are, in particular, the great Revenue offices. They are two in number, one governed by the Board of Commissioners of Inland Revenue, and one by the Board of Commissioners of Customs and Excise. The

first lives in that fine house which stands upon the site of the one-time palace of the Dukes of Somerset on the Embankment. Its work is to collect the direct taxes, the taxes that are assessed upon the general taxpayer and collected from him directly. Taxes are mutable things: both their bases and their rates may and do change from year to year, and it is not within the scope of this book to give a detailed account of their nature. Existing taxes may be changed or abolished, or new ones added, but whatever direct taxation has to be collected, it is this Board that collects it. At the head of the Department there is a Chairman, a permanent civil servant of high standing, and often one who has been transplanted to Somerset House from the Treasury. To help him there is a Deputy-Chairman, and the "Board of Inland Revenue" is made up of these and the two Secretaries, who act as Commissioners. Under these there are various sectional sub-divisions, of which we need notice only a special financial sub-division, the office of the Accountant and Comptroller General under an officer bearing that title.

The office of the Commissioners of Customs and Excise is at the vast warren of the Custom House in Lower Thames Street. A strong and universal smell of tobacco bears witness there to the nature of its work: it is to collect the indirect taxes, which are the customs duties levied on goods brought into the country and excise duties levied on goods produced within the country. Until April 1, 1909, the collection of excise duties was in the hands of the Board of Inland Revenue. Only since then have the Commissioners of Customs been Commissioners of Excise also. Of indirect taxes,

as of direct taxes, we need give here no detailed account. Whatever the customs and excise duties may be, it is for this department to collect them. In addition it has a variety of miscellaneous tasks to perform which have been left to it at various times because of its widespread net of local officers. Of these the local administration of the Old Age Pensions Act is the most laborious; but such activities are not strictly connected with the special function of the department in the financial organism, which is that of a collector of revenue. The organisation of the office is similar to that of the Board of Inland Revenue. There is a permanent civil servant of high standing at its head as Chairman, and part of the domestic organisation is a financial department under an Accountant and Comptroller General. Another part of its organisation is a Statistical Office, which records and prepares for publication the statistics of exports and imports, shipping, and so on: it has an important financial function to perform in the preparation of estimates of revenue.

It is to the Treasury Ministers that the two great revenue-collecting departments report. They are responsible to them and subject to their authority.[1] They have no ministers or parliamentary representatives of their own: the Chancellor of the Exchequer and the Financial Secretary of the Treasury, and on minor matters always the latter, speak for them in the House of Commons. In the same position are several other and smaller departments, whose work is much concerned with the collection of revenue or other financial affairs. A revenue collector and something more besides is

[1] Customs Consolidation Act, 1876 (39 & 40 Vict. c. 36), § 2.

the office of the Commissioners of Woods, Forests, and Land Revenues, which has a modern building to itself in Whitehall. It manages the lands of the Crown, which are now treated, not as the Crown's private property, but as the lands of the state. It collects the rents, provides for upkeep and repairs and so on, and pays in as revenue the profit-balance. So the office represents the state as landlord. There are two commissioners, of whom the first as a rule is the Minister of Agriculture. The other commissioner is a paid and permanent civil servant.

There is another great revenue-collecting office, the Post Office, making four in all; but that is not under Treasury Ministers. It differs from the other Revenue departments in that the surplus which it pays into the Exchequer after meeting the cost of posts, telegraphs, and telephones is a very small fraction of its total receipts. Even so we are more fortunate than the many countries whose Postal Services do not even pay their way. Next in the list of the Treasury's connection we come to an office with high and independent functions to perform in the financial organism, which is nevertheless in specially close touch with the central financial department. It is the Exchequer and Audit Department, presided over by the Comptroller and Auditor General. With its functions, which are the control of Exchequer issues and the audit of public accounts, we shall be much concerned hereafter. The department has intimate relations with the Treasury, whose ally it is in the supervision of expenditure. But its head is wholly independent. He is not subordinate to the Chancellor of the Exchequer: he is an officer of the House of Commons and answerable to that alone.

The Royal Mint is an immediate dependent of the Treasury in the financial organism. It is the national coin-factory. In its sombre and ancient quarters by the Tower of London it coins gold and silver and copper to meet our needs for cash, under the immediate control of Treasury Chambers. The Chancellor of the Exchequer is its Master, and its figure-head. In everyday life it is under the control of his principal Deputy Master on Tower Hill, and others at the branch mints at Sydney, Melbourne, Perth, Ottawa, and Pretoria.

An office of great importance in the financial scheme which is within the Treasury's immediate sphere of influence is the National Debt Office, which is the office of the National Debt Commissioners. It does not manage the National Debt; that is the work of the Bank of England. Its function is to carry on the business of buying and selling Government stocks for Sinking Funds and for the various Government departments, such as the Post Office, which have funds to invest. So it is the Treasury's representative in the City, and it is in the City that it has its quarters, in Old Jewry, next door to the Bank, where the Bank has provided it with premises which are up to the City's standard of magnificence. The Commissioners exist only in name. The office in practice is directed by a Comptroller General, who is a permanent civil servant. Last in the list of the Treasury's special charges may be mentioned the Office of Works and the Stationery Office. They are under the Treasury's direct control, but they have no special or peculiar functions to perform in the financial organism, beyond spending money like every other Government office, and so they need not delay us.

We will pass on to the great spenders, the pipes through which the public money runs back into use after it has been pumped out of use through the Revenue departments. The chief of these are the War Office and the Admiralty, and here we emerge from the region of the Treasury's suzerainty. The new and expensive cupolas of the War Office in Whitehall Gardens and the tall red ranges of the Admiralty on the Horse Guards' Parade owe no allegiance to Treasury Chambers at their feet. We need not burden ourselves with a detailed account of the elaborate organisation of these great emptiers of the nation's purse. One circumstance only needs emphasis; that each has within it a special financial organisation, more or less independent of its executive organisation. The War Office contains within it a financial department called the Department of the Finance Member of the Army Council. That finance member is the Financial Secretary of the War Office, who is a politician and a member of the Ministry. Under him the permanent head of his Department is the Secretary (Finance), a Civil Servant who is a member of the Army Council, and presides over the labours of three Principal Assistant Secretaries known as Directors of Finance, and many Assistant Secretaries, Principals, Accountants, Paymasters, and Clerks, all engaged on financial business. The Admiralty has also a parliamentary Financial Secretary, with a Permanent Assistant Secretary for Finance Duties. The accounting work of the office is under a permanent official who bears the title of Accountant General.

Finally, and to complete this sketch of the groups of officials who carry on the nation's financial business, there must be mentioned an office which, little heard

of by the public, discharges nevertheless functions of the first importance: it is the Pay Office; in full, the Office of His Majesty's Paymaster General.

Neither the great spending departments, the Admiralty and the War Office, nor the small ones, the Civil Service departments (with an important exception to be mentioned) are makers of their own payments. Payments are made for them by the Pay Office. Over it presides a high dignitary, the Paymaster General, but he is a *roi fainéant*. A political and unpaid officer, he has fulfilled all the duties which he ever does fulfil when he has signed an authority for an assistant to act for him. The Assistant Paymaster General, the real head of the office, like the Deputy Master of the Mint and the Comptroller of the National Debt Office, is under the direct control of the Treasury.

Such are the men by whom the financial affairs of the state are conducted. They fall into three groups: the collectors, the spenders, and the Treasury (with its auxiliary the Exchequer and Audit Department and its subsidiary the Pay Office) which watches, advises, checks, and co-ordinates the whole. At the root of the system of organisation a certain parallelism may be seen, not designed, but the result of a slow evolution adapting the machinery to meet its needs. It is a parallelism between executive control and specialised financial control. Parallel with the executive departments is the financial control of the Treasury. Within each great department, again, which has financial functions to perform, whether getting or spending, parallel with the executive staff there is the financial staff and the accountants' department. That illustrates what may be described as the first

principle of good financial administration, that all executive officers who have financial duties to perform, and above all the spenders, need an independent officer to watch them whose business it is to enforce economy. It may not be obvious that it is so in theory; our system is a living witness of its great desirability in practice.

The executive officer who is not a mere sluggard, the man who has work to do and wants to do it, must always be thinking of how to widen the sphere of his influence and activities, how to get as much as possible to do, and how to get it done most completely and quickly. It is asking too much of human nature to expect him to put economy first, when that might narrow his sphere of influence, take the polish off his products, or cost him time and trouble. But economy is a necessity, however tedious and however unpopular. It must be enforced at every stage, because extravagance in one department must ultimately prejudice its own work or that of some other, and extravagance in all departments must reduce the total amount of work which the state can do. If the work of enforcing economy is to be done with efficiency, human nature being what it is, it cannot be left to those whose power and reputation depend upon spending; it must be given to somebody else to do, whose whole work it will be and whose power and reputation will depend upon his efficiency in economising. Hence the need for a division of functions and for an independence as great as possible in the position of the economiser. In an ideal administrative system every executive department would have its financial side, dependent only upon the head of the office, armed with full powers to examine, advise, and remonstrate, and

empowered to communicate through its sectional chief with the departmental chief. We have that for the civil service as a whole in the Treasury. We have it for the Admiralty, War Office, Air Ministry, and Revenue Offices, in different degrees which will need more particular attention hereafter, in their special financial branches. In other offices we lack any such check, but other offices are of less financial importance. The Treasury can do the work of financial critic well enough for all but the great spending departments. In their vast, complex, and growing organisations, the most effective agent for economy must be one domestic, ever-present, and well-versed in the internal affairs of the office. In the case of the Admiralty, War Office, and Air Ministry, the independent financial side within the office is the best and only guarantee of a rigid economy in details, and it is in details that money is wasted. Rather is it, perhaps, a guarantee that the supreme head of the department has at any rate the opportunity of enforcing economy in details, because unless, of course, the Minister is an economist at heart his departmental watchman waketh but in vain.

To maintain and increase the independence of those independent yet domestic financial sections should be the care of the good administrator. Complete independence, it may be admitted, they cannot have. The work of the offices has to get itself done, and it would be demoralised were the chief financial officer of the department to have a power of absolute veto. He must be subordinate to the parliamentary head of the office; but it is enough if he be that. He should be subordinate to no one else therein. His staff, moreover, should be in direct contact with

the executive staff, helping with its financial knowledge, advising, admonishing, and carrying high questions of economy forward to the head of the office through the financial head. It is only thus that it can be of much real use. As a body of mere accountants and recorders the value of its work is less, because it is done after the event, when the money is spent or the nation is committed to spending it. To get the full benefit of a financial staff it should be in a direct, active, and constant touch with the executive, locking stable doors while the contents are still in the stalls.

# CHAPTER II

## THE ESTIMATES

In the classic maxim set upon the title page of this book, Mr. Micawber summarises and illustrates the whole theory of state finance as it ought to be; and his practice is no less illustrative of state finance as it too often is. Having disregarded its own good rules, the improvident state finds itself in the King's Bench with a deficit, borrows a shilling for porter, and cheers up. Against such financial tribulations foresight is the only protection. A virtuous state that wants to keep out of gaol must look ahead; it must not wait for something to turn up. Before it embarks upon the business of the year it must calculate what expenses it will have to meet and make plans to meet them. Ours, being a virtuous state, does so by means of forecasts of expenditure called Estimates.

### Preparation of Estimates

The very first step in the financial arrangements of a year is the preparation of estimates of the expenditure to be met. To approve them is the work of the Legislature, but to prepare them is that of the Executive. Parliament will have the last word upon them, but Parliament cannot of course itself make them out: for that the detailed knowledge

of the Executive is needed. First of all the responsible Ministers must make up their mind on the broad matters of policy which affect expenditure. We may picture them as feeling their way tentatively with the Chancellor of the Exchequer, and finding out what they can get without a pitched battle. Then the departments can prepare details of the expenditure needed to effect the purposes of the Ministers, and to carry on the Government, in the light of the experience of preceding years. Lastly the detailed estimates are presented to Parliament for its consideration.

In logical order, as in order of time, the preparation of the Estimates is the first part of the nation's annual financial business to be considered; and it is not only the first but by far the most critical. Both in form and substance the estimates are the foundation of the whole financial structure of government. In form they are the basis of the national accounts; as services are sorted out in the estimates, so are they sorted out in every account kept thereafter during the year.

Everything as regards efficiency and economy in public expenditure depends upon the preparation of the estimates. Theoretically, Parliament has the right and opportunity to criticise and amend them. Actually, so enormous is their bulk and intricacy, so wide and varied is the special and technical knowledge needed for an understanding of their details, so timid in consequence are the non-professional members of the House of Commons of suggesting or making alterations, that the changes made in the House of Commons are commonly very slight. Once a thing is down in the estimates as presented to the House, it is a hundred to one that it stays there.

Small matters are overlooked, large matters become party questions by which the Government stands or falls. Nowadays, in short, the theoretical responsibility for our national expenditure may still be with the Commons, but the work is too much for them, and it results that the practical responsibility is with the departments which prepare the estimates, each under its Minister. The manner in which the estimates are prepared is therefore of the greatest concern to every taxpayer. It is at the time when they are being discussed and formulated in detail in the departments that economies can be made in his interest; when they are being passed in Parliament in blocks and undiscussed it is too late. Once the estimates have been published by the departments which draw them up the taxpayer's fate is sealed.

Let us then trace this vital process in some detail. April 1st is the beginning of the financial year. To allow time for the Government to make its financial plans well beforehand, the estimates for the year are taken in hand in the preceding autumn. The Treasury, the co-ordinating department which has the general superintendence of all financial administration, is the moving spirit. On October 1st it sends a circular letter to the officers responsible for the preparation of the estimates in each civil department, requesting them to prepare estimates of the expenses of the departments in the coming year. There are two stereotyped admonitions in this circular: one is general, that the state of the public revenue demands the utmost economy; the other is a particular warning against assuming last year's estimates as the starting point for those of the next. The latter is a necessary warning. It must always

be a temptation to one drawing up an estimate to save himself trouble by taking last year's estimate for granted, adding something to any item for which an increased expenditure is foreseen. Nothing could be easier, or more wasteful and extravagant. It is in that way that obsolete expenditure is enabled to make its appearance year after year in the estimates, long after all reason for it has ceased to be. By this warning and by the general admonition as to the need for economy the departments are no doubt duly impressed.

A start having been made by the Treasury's letter, the responsible officers set their staffs to work at getting out the estimates for their departments. In every case it is the department which will be responsible for the spending of the money that is responsible also for the preparation of the estimate; as the department makes its bed, so will it lie on it. In the case of the estimates for the Civil Service and Revenue departments the procedure of preparation differs from that in the case of the Navy, Army, and Air estimates. Let us consider the Civil Service estimates first. For these the Treasury itself has a particular responsibility; it is the Financial Secretary of the Treasury, as understudy to the Chancellor of the Exchequer, who presents them to Parliament, although it is the Ministers of the departments who look after their respective estimates after they have been presented. The Treasury does not of course prepare them itself; it would not have the necessary knowledge. That work is done in the departments, but it is done under the close supervision of the Treasury. With its letter early in October the Treasury sends to the Civil Service departments forms of estimate, showing

the last year's figures, with blanks left for the estimated figures for the new year. They make out their estimates in detail, obtaining if necessary subsidiary estimates from their branch departments. Having made them out, they transmit them to the Treasury. The bulk of them reach it between December 1st and an early date in January. An explanation of each goes with it from the department which prepared it, and a note of the particulars for which Treasury sanction is still required. At the Treasury the estimates are examined and checked by a special official of standing, the Estimates Clerk. They are then submitted to the Financial Secretary for his approval. In general the Treasury criticises, suggests, and amends, and in any difference of opinion with the department which prepared the estimate it has the last word. Having run the gauntlet at the Treasury, having been subjected there to a detailed examination and gained a final approval, the Civil Service estimates are ready for presentation to Parliament.

The Treasury's criticism of the Civil Service estimates and its decisions on the new points which arise thereon are not confined to the period between its receipt of draft estimates from the departments and their presentation to Parliament. Were it so its control would be of little value; time would not serve for a careful examination, and after the estimates have once been cast into form, even as a draft only, it is harder to make alterations in them than before. As we have seen, each Civil Service department is correlated with two of the Divisions of the Treasury presided over by an Assistant Secretary. In fact a great part of the relations between the department and its Treasury

friends in the course of the year consists in the discussion of questions concerning the next year's estimates, an increase in staff here, it may be, or in pay there, or in a grant somewhere else. All the year round the Treasury Divisions are thrashing out questions of expenditure and economy each with its group of departments. So, when the estimates come to be prepared, as regards most of the changes in them the departments have only to embody the result of conclusions already come to by the Treasury and themselves, and the Treasury has only to see that the course which it has decided upon is followed. Sometimes, it may be, a department will make the actual preparation of the estimates an opportunity to have another try for something that it has been refused.

Over the Civil Service estimates the Treasury exercises in this way an effective control: as the business of government grows, and expenditure with it, the control must become more difficult of maintenance; but it is still a practical and substantial check upon extravagance. Over the estimates for the Navy and Army its control is much less. Since their preparation fixes the amount of the taxpayers' most onerous burdens, and now, in the permanently congested state of parliamentary business, fixes it irrevocably, it is worth while to consider the process in some detail.

At the Admiralty the ball is set rolling by the First Lord, who directs the departments responsible for the several Votes to prepare a sketch estimate for the coming year. Guidance on matters of high policy, such as the programme of ship-building, is obtained by each branch from its head, in consultation with the Board of Admiralty. A sketch is

made out of each Vote, and is submitted to a central Admiralty Finance Committee. The Committee co-ordinates the whole, considers in conjunction with the Superintending Lord concerned what is the justification for each item and what economies should be made, and sends the general sketch estimate Vote by Vote with its report in detail to the First Lord. In the process of preparation of the sketch estimates, the last stage is the First Lord's revision in the light of the Committee's report. He fixes the total of each Vote of the sketch, and thus arrives at a grand total which he communicates to the Chancellor of the Exchequer in November or December, in a letter explaining the chief differences between the new estimate and its predecessor (and stating the total amount to be required). Now should high debate take place upon the policy of the Estimates between the champion of spending and the champion of economy. According to the great Gladstonian tradition it is the function of the Chancellor of the Exchequer to act towards the estimates of spending departments as *advocatus diaboli.* As guardian of the people's purse and as the man who will have to find the money, it is for him to see that no service is included that is not essential, and that every service that is included is provided for in the most economical manner. After all has been done that can be done by mutual concessions, unreconciled differences between the Chancellor and spending ministers are left to the decision of the Cabinet and of the Prime Minister. How far this great tradition of the nineteenth century, that makes the Chancellor the watchdog of economy, has been maintained in the twentieth century will be for its future historian to say. One thing is clear: that the power and utility

of the Chancellor in this respect must be affected by any development in our system of government which allows him the initiative in schemes of fresh expenditure.

When the First Lord, the Chancellor, and the Cabinet have come to an agreement about the sketch estimate, it goes back to the Admiralty. The estimating departments of the office take it up again and work out the sketch into the draft of a detailed estimate. This draft passes through the same stages as the sketch. It is prepared by the responsible departments, criticised and revised by the Departmental Finance Committee, and revised and approved by the Board of Admiralty and the First Lord. Passed by them, it becomes the final estimate, and it is submitted to the Treasury for its ratification. This final step is now little more than a formality. Already when the estimate reaches the Treasury it has been considered and approved in all essentials by the Cabinet. It is little likely that after that the Treasury will think it worth while to make much remonstrance on questions of substance.

At the War Office the estimates are prepared in much the same way as at the Admiralty. In November, the Financial Secretary fixes a day by which the departments should send to him their sketch estimates. Then, in the departments, sketch proposals of their requirements are prepared by the financial advisers of the executive officers, under the directions of the members of the Army Council. Their proposals are collated by the heads of the financial branch. In consultation with the Army Council, the Secretary of State thrashes the matter out with the Chancellor of the Exchequer, and agrees a total. An agreement having been arrived

at between them, the sketch estimates come back to the War Office. Meetings are held of the members of the Army Council and the heads of the financial staff of the office. The Secretary of State gives directions as to general policy, and the estimates are cut down to the amount available. Finally, the executive departments elaborate the sketches into a full draft estimate; the Secretary of State passes them; and they go in their final form to the Treasury for its formal ratification.

Such is the process by which the Executive determines the demands which it will make upon the taxpayer. In the chronic congestion of parliamentary business, the demand once made and the form of the estimate fixed, the thing is practically settled. If economy is to have its say, it must be before the estimates are taken in hand and while they are being made out. In this connection economy has two chief functions. It must see that no services are included that are not needed, that is economy in matters of policy: and it must see that in the provision for needed services there is no extravagance, that is economy in matters of detail.

The Estimates for the Civil Departments are less affected than those for the Navy and Army by broad questions of policy. New spending on civil objects is usually a matter for initiation by an Act of Parliament. Such liabilities as those incurred for Old Age Pensions do not make their first appearance in an estimate. In the other particular, economy in detail, the control which the Treasury has over Civil estimates under the system described is more than formal. By means of its close relations with the Civil departments all the year round, the Treasury can exercise in their case a very efficient check on

waste, and can enforce its measures by its active scrutiny of their draft estimates.

But it must be apparent from what has been said that with the Navy and Army estimates it is otherwise. Many matters of high policy which may lead to large new expenditure make their first appearance therein. It is by the naval estimates, for instance, that the country is committed to building an additional battleship, and that costs round millions. Over such high matters the Treasury, as a department, exercises less control. The external restraining force for economy, parallel to the spending force of the executive branches of the department, is the Chancellor of the Exchequer.

Naturally, and perhaps inevitably, with the increase in the volume, intricacy, and technicality of the business of the great spending departments, the external control of them by the Treasury has weakened. It has passed to other hands. As Treasury control has weakened, the Admiralty and War Office have had themselves to undertake control and surveillance of themselves in matters of finance. The necessary work of parallel and independent restraint on the spending of the Admiralty and War Office, which the Treasury used to do, is now done to a large and increasing extent by their own internal financial branches. As the adviser and helper of the executive spending branches of an office, a well-organised internal financial branch has great advantages over an external power like the Treasury. It has more intimate association in daily intercourse with the spenders, and it has the detailed and technical knowledge of their work, lack of which has been the chief reason for the enfeebling of Treasury control. On the other hand it is at one great disadvantage in

comparison with an external power, that it is not wholly independent.

Since the reality of financial criticism and control over the chief heads of expenditure has thus passed into the hands of the internal financial branches of the Admiralty and War Office, it is worth while to consider the conditions under which they can best do their work as economisers. We are dealing here with one part only of their work, but that which is also the most vital, the services which they can render to economy at the time when the expenditure for the year is being crystallised by the preparation of the estimates. Later we shall have to apply what is said here to the other chief part of the work, that of checking waste in actual expenditure. In the first place, it may be said that the first condition for efficiency in the work of the financial staff is that it should labour, not at arm's length from the executive, but in organised connection with it. It is clearly not enough that it should be a mere body of accountants and book-keepers, working in isolation: it should be a body of financial advisers also, taking part in the every-day work of the executive staff. When the estimates are being prepared, for instance, it should have a say for economy in their preparation. By working all the year round in close touch with the executive staff the financial staff must gain an equipment of technical knowledge, and by that the advice which it gives at the critical period of the crystallisation of charges must gain greatly in weight. In the second place, the financial staff, although working in organised connection with the executive, should be independent in the official hierarchy of the authority of executive officers,

and subject only to that of the permanent chief of the financial side of the office; and he in his turn should be subject only to the authority of the minister and in direct communication with him. That is needed in order that criticisms and representations may travel unintercepted straight from subordinate financial officials to the top. Once objection is taken by the financial staff, it should be in the power of no executive and spending officer, except the minister, finally to overrule it. Thus the position of the financial officers working in connection with the executive branches of the department should be that of ambassadors from the financial chief; and the financial chief should be the minister's *alter ego* for economy. In this way may be secured the greatest possible independence in the internal and parallel financial control which is consistent with a necessity greater than the necessity for economy, the necessity that the work of the office should be got done. That pre-eminent necessity is secured by the subordination of the financial chief to the minister. An absolute power of veto, it must be recognised, he cannot have, or a power of appeal to an external authority such as the Treasury. By the first the public service might be brought to a standstill. The second might be the cause of infinite friction, and would impair in the most undesirable manner the responsibility of the actual spenders for economy in their expenditure. There must be full responsibility for expenditure in the department and its minister; but under the minister, the financial staff, although dovetailed with the executive staff in its daily work, should be independent of it in authority.

Finally, great as may be the influence of a strong

and well-organised departmental financial staff, let us not exaggerate it, or suppose that it can do much without the good will towards economy of the supreme head of the office. It is his watch-dog, and no more, and the best of watch-dogs is of little worth if its master refuses to be awakened by its barking. Unless the minister realises that economy is the better part of efficiency, his financial staff is working at a lever without a fulcrum. But even so it serves a purpose of a sort. It makes him effectually responsible for his decisions on questions of expenditure; it prevents him at least from running blindly into extravagance at the bidding of the spenders.

### Estimates of Revenue

Having calculated what it will have to spend in the course of the coming year, the prudent state, like the prudent householder, must calculate what income it will have with which to meet its outgoings. It must estimate its revenue as well as its expenditure. For the plan of campaign to raise revenue to meet the estimated expenditure the Chancellor of the Exchequer and, under him, the Treasury are responsible. The plan is called by the familiar name of the Budget. Estimates of the revenue to be derived in a coming year from existing taxes and any proposed increases therein or from new taxes are prepared for the Treasury by the Revenue departments. Their preparation is work for those with expert knowledge and especially for statisticians, and the greater part of it is done by the Statistical Office of the Board of Customs and Excise. There they have records of the yields of

all taxes for many years, which show their normal rates of increase with growing wealth and population, the effect of any change in rates, and that of any special circumstances such as strikes, wars, and unusual weather. By taking last year's yields as a basis, adding or subtracting a normal amount for the regular increases or decreases which the records show to be in progress, and making a correction for any abnormal disturbing influence which it is possible to foresee, a very exact estimate can be made of the revenue in the coming year. Armed with that, the Chancellor knows as well as man can know how he stands, and how he may best meet the demands of the spending departments.

### Treasury Powers

One great advantage of the work done for economy by the financial branch within an office over that done from without is that, being done with intimate knowledge of the needs of the executive and in close personal contact with it under one roof, it can be treated as a friendly help rather than as a hostile check. Something of the latter element must always enter into the external control of the Treasury. It is inevitable that there should be some institutional jealousy between the spending departments and the saving department over the way. To reduce the friction as much as possible, the sphere of Treasury intervention must needs be defined by rules and limited to matters of first importance, and those which lie within its special sphere, such as scales of salary. An outside office interfering unnecessarily in the details of the administrative work of other

offices would soon create friction enough to bring the machine of government to a standstill. Another mischievous effect which it would have would be to deprive the actual spenders of responsibility for their expenditure, and to transfer it to a body without the means of information or control necessary to enable it to exercise that responsibility with efficiency.

The Treasury's province in financial control is then, and ought to be, clearly defined. Within that province, it may be repeated, its operations go on all the year round by correspondence and daily personal consultations with the departments, and the decisions arrived at are embodied in the next estimates. Its first and foremost function is to consider and judge any proposal made by a department which would have the effect of imposing a new or an increased charge on the public purse. New charges and changes of the sort divide themselves into two chief classes. One includes charges for establishments; the other includes charges for grants, and purchases. Over the latter class the control of the Treasury must in the nature of things be weak. Grants of the larger size, such as education grants and grants in relief of local taxation, are for the most part fixed by special Acts of Parliament and are thus removed from the sphere of the Treasury's influence. Amongst purchases are included such big affairs as the outlay for naval construction, which are decided in principle in the Cabinet, and over which the control of the Treasury is thus reduced to a formality. Moreover, about the expediency of fresh grants and fresh purchases during the coming year the responsible executive officers alone can have the knowledge necessary for judgment. If somebody

at the War Office says that the future of the race depends on having Smith's range-finders at ten guineas instead of Brown's at five, who at the Treasury shall say him nay?

In contrast with such affairs as these, the class of establishment charges is that over which the control of the Treasury and its influence for economy are most close and efficient. Every change in the organisation of the public service which involves a present or future increase in the charge on the public purse needs the assent of the Treasury. If for instance a new post is to be created, or a salary is to be increased, the Treasury must be consulted and its assent obtained. That is perhaps the Treasury's most characteristic activity. It is the taskmaster of the servants of the state, charged with the necessary but ungrateful task of requiring from each a fair day's work for a fair day's pay. This is, however, but a single instance of its general function in financial control, which is to see that the rules of financial order are kept by the departments of the Civil Service, and that there is no negligence, indolence, or obliquity in their observance by the servants of the public. Other characteristic instances of the functions performed by the Treasury are its duty to see that no claim once advanced by a department is abandoned, and that no stipulation in any contract made on behalf of the state is waived without its express permission. No payment, for instance, may be made to a contractor in contravention of or beyond the terms of a contract without Treasury sanction. In considering questions of the sort the Treasury must of course be guided in technical matters by the executive officers of the department which makes an application for its sanction; but it adds to their

special knowledge its own special care for the interests of the public purse. Suppose that the Admiralty, in its contract for the construction of a warship, has stipulated that the ship must pass certain trials before payment is made for it, and suppose that it has changed its mind and wants to accept the ship and to pay for it without insisting on the trials: here there is a contract to be varied, and the sanction of the Treasury is needed. It is true that the Treasury cannot be expected to judge the merits of the case and to have an expert opinion whether the ship ought to be accepted without the trials or not: but the need to obtain its sanction in order to dispense with the trials serves one good purpose: it secures that the Admiralty's reasons for dispensing with them shall be placed on record, and that they shall be at least good enough to convince the ordinary and inexpert man that the sole motive for dispensing with them is the public interest. In general indeed the object of the Treasury's control is not mere obstruction, it is not to say "no" whenever "no" can be said, and to cut down anything and everything. Rather is it a means to secure that whenever a department sees fit to take something in the nature of a financial liberty its reasons for taking it shall be recorded and that they shall seem good on the face of them to an onlooker who is prejudiced, if at all, in favour of economy. Day by day throughout the year the Treasury is discussing and deciding questions of this kind raised by applications from the departments. When the time for the preparation of the estimates comes round, the increased charges which it has allowed in its decisions are included in the estimates, and those which it has refused are excluded.

## The Form of the Estimates[1]

It has already been observed that the form in which the estimates are cast has a special importance, because it is the foundation of the whole system of public accounts for the year. Expenditure is accounted for according to the system and the classification that are established in the estimates considered by Parliament. Generally speaking, the form of an estimate is that of a double column. In the first a service is described; in the second the sum to be spent upon that service is specified. The services are classified in groups, called Votes. They are called Votes because each group of the sort is made the subject of a special vote of the House of Commons in Supply. Votes are the units of the national accounts.

The present form of estimates, and in particular their division into sub-heads, the content of which receives the formal approval of Parliament, is very well adapted for the exercise of financial control over the aggregate payments by a department in respect of each of the more or less homogeneous groups of services of which a sub-head is made up. But this grouping is not always that which affords the best basis for a reasoned criticism of public expenditure. As the system now stands, to take instances at random from the estimates, we can see at a glance the total salaries of the Home Office, the total cost of paper and printing for the whole Civil Service, or of accommodation for certain classes of it (subdivided into new building works, maintenance and repairs of existing buildings, furniture,

[1] An example of a Vote in the Estimates will be found in Appendix A.

etc.). But it is not possible for the Cabinet itself to find out, without a lengthy collection and analysis of detailed figures, the whole expenditure on any given object—including the headquarter and other staff employed in connection with it, the buildings from which it is administered or in which it is housed, and the stationery used for and about it.

The existing system has been criticised for this failure to show the cost and financial position of any service as a whole, by the Select Committee on National Expenditure, who in 1918 recommended that it should be replaced by a system modelled on the cost-accounting of commerce. This has been done, in the form indicated by the specimen extracts in Appendix B., in the Army Estimates for the last three years, but it is not yet apparent whether the increased cost, complexity, and delay, and the difficulties of comparison with the years before the introduction of the new system, are outweighed by substantial advantages which would justify the extension of the new accounting to any other departments.

It will be observed that under this system there is only one single Vote for the whole of Army services; the subdivisions are heads of expenditure, divided again into sub-heads. In these is gathered together all expenditure which is relevant to a given service, no matter by what department or branch the ancillary services are administered.

Changes in the form of the estimates affect the whole subsequent business of accounting throughout the year; and were changes to be made by the departments too frequently, without notice, or in an ill-considered manner, it would introduce great uncertainty and confusion into the nation's accounts.

It would impede also the process of direct comparison with the estimates of preceding years, and that is one of the most valuable safeguards of economy. For that reason it is a rule that no substantial change in the form of its estimates may be made by any department without the previous sanction of the Treasury.

### Appropriations in Aid

For clearness' sake we must consider here a certain special feature in the estimates, although strictly speaking it is a matter rather of accounts than of estimates. Taxes are collected by the great Revenue departments alone, but in addition to that almost every other department receives various small sums in the course of the year which are paid to it as casual incidents of its administrative work. Formerly the greater part of these was paid by the receiving departments into the Exchequer Account at the Bank of England. A small part of them is still dealt with in that manner. But in the belief that it is simpler and more economical to use these funds where they come to hand the departments are now, for the most part, allowed to retain them and to appropriate them in aid of their expenditure.[1] Appropriations in Aid is the name which is given to them accordingly. There is no absolute uniformity in this matter. In the cases of the Admiralty and War Office and most of the Civil departments the whole of the minor receipts of the department are thus appropriated. Minor receipts of a few of the Civil departments are still paid straight into the

[1] Cf. Public Accounts and Charges Act, 1891.

Exchequer Account. When estimating its expenditure for the year, each department which receives appropriations in aid has also to estimate, Vote by Vote, what sums it will receive in the course of performing the services included in that Vote. Its estimated receipts are entered in the Estimate for the Vote as a final sub-head of account under their name of Appropriation in Aid. Estimated receipts are deducted from estimated expenditure, and the balance is the sum to be voted by Parliament.

# CHAPTER III

## MONEY IN PARLIAMENT

IN our system of government, the executive power is in the hands of the officers described in the first chapter, acting under the supreme control of the Cabinet. They it is who do the nation's financial work of collecting the revenue and of spending it. But before that can be done, it has to be decided how much is to be collected and from whom, and on what it is to be spent, and that is the work of the Legislature. Before a penny can be extracted by the state from the pocket of a taxpayer or a penny spent or a pennyworth of liability incurred, a law must be passed to authorise it, and it is only the triple Legislature of King, Lords, and Commons that can pass the law. The principle has the most distinguished origin; it is one of the few actually rooted in Magna Charter, out of the many which are traditionally supposed to be. "No scutage or aid," swore King John at Runnymede, "shall be imposed in our kingdom unless by the general council of our kingdom"; and what the general council was then Parliament is now. The Bill of Rights is another of its noble ancestors. "Henceforth," it was declared in 1688, "shall no man be compelled to make any gift, loan, or benevolence, or tax, without common consent by Act of Parliament;" and the unlawfulness was pr

of levying money "for and to the use of the Crown by pretence of prerogative for other time and in other manner than the same was granted by Parliament." The Crown, as will be seen, has special privileges allowed it in the sphere of financial legislation, but Magna Charter and the Bill of Rights leave no room for any confused idea that the Crown has any shred of prerogative to impose or increase taxation, or to alter its incidence, independently of Parliament. Runnymede was the beginning of the end of prerogative imposts, and the Revolution was their grave. A small private revenue is still derived by the Crown from several landed estates; but its public revenue is dependent on Acts of Parliament, annual or permanent.

## Lords and Commons

Nor are the two Houses of Parliament equal in matters of money; the House of Commons is paramount. There sit the representatives of the taxpayers, and in the course of a long historical struggle they have won for themselves exclusive control over the raising and spending of money. Their financial rights and privileges in their relations with the unelected House were first defined by their own resolutions. When Naseby had settled the contest between Crown and Parliament for financial sovereignty, there began a peaceful conflict between the two Houses which lasted into our own times. It soon came to a head. In 1678 the Commons resolved in the ample phraseology of the times "that all aids and supplies and aids to His Majesty in Parliament are the sole gifts of the Commons and all bills for the granting of any such aids or supplies

ought to begin with the Commons, and that it is the undoubted and sole right of the Commons to direct limit and appoint in such bills the ends purposes considerations conditions limitations and qualifications of such grants, which ought not to be changed or altered by the Lords." Thereafter the attacks of the Lords upon the rights thus claimed were more flank attacks than frontal. No open conflict broke out again until the dispute over the paper duties in 1860, when, moved thereto by Gladstone, the Commons passed a series of three resolutions which codified their claims. They resolved, *ore rotundo* :—

"That the right of granting aids and supplies to the Crown is in the Commons alone, as an essential part of their constitution, and the limitation of all such grants as to matter manner measure and time.

"That although the Lords have exercised the power of rejecting bills of several descriptions relative to taxation by negativing the whole, yet the exercise of that power by them has not been frequent and is justly regarded by this House with peculiar jealousy, as affecting the right of the Commons to grant the supplies and to provide the ways and means for the service of the year.

"That, to guard for the future against an undue exercise of that power by the Lords, and to secure to the Commons their rightful control over taxation and supply, the House has in its own hands the power so to impose and remit taxes, and to frame bills of supply, that the right of the Commons as to the matter manner measure and time may be maintained inviolate."

If the chaff be winnowed off the grain of these resolutions, it will be seen that they claim absolutely for the House of Commons two privileges: they

claim that the Commons have the sole right of initiative in taxation, and that they have the sole right of determining its manner and measure. To these claims the Lords, tacitly at least, assented, agreeing that money bills must begin in the Commons, and that the Lords should not amend them. The resolutions also advanced another theory, but scarcely made a claim of it; that the Lords have no business to reject a money bill. To this the Lords never agreed, and in 1909 they gave expression to a very emphatic disagreement by their historic act in rejecting the Budget of that year. There followed the great conflict between the Houses which, after two general elections, was brought to an end by the Parliament Act of 1911. By that the House of Lords is deprived of the power to reject a money bill. By the first section, "if a money bill, having been passed by the House of Commons, and sent up to the House of Lords at least one month before the end of the session, is not passed by the House of Lords without amendment within one month after it is so sent up to that House, the bill shall, unless the House of Commons direct to the contrary, be presented to His Majesty and become an act of parliament on the royal assent being signified, notwithstanding that the House of Lords have not consented to the bill." [1]

[1] 1 and 2 Geo. 5, c. 15, § 1, ss. 1. By § 1, ss. 2 and 3, it is provided that "a money bill means a public bill which in the opinion of the Speaker of the House of Commons contains only provisions dealing with all or any of the following subjects, namely, the imposition, repeal, remission, alteration or regulation of taxation; the imposition for the payment of debt or receipt, custody, issue or audit or account of public money; the raising or guarantee of any loan or the repayment thereof; or subordinate matters incidental to these subjects or any of them.' There shall be endorsed on every money bill when it is sent up to the House of Lords and when it is presented to His Majesty for assent the certificate of the Speaker of the House of Commons, signed

Such is now the law of the matter. The Act also contains a declaration (in Section 6) that "nothing in this Act shall diminish or qualify the existing rights or privileges of the House of Commons," so that the resolutions of 1678 and 1860 have still such authority as a resolution of a single House can have. To them we must refer, in particular, for a declaration of the Commons' privilege of initiative in taxation, a privilege which is now fully recognised by the Lords. If it is found convenient to introduce in the Lords a bill which imposes a charge, that House, to avoid a breach of the Commons' privileges, takes refuge in a very artificial device. When it is reading the bill a third time it leaves out the financial clauses which impose the charge, but it prints them in a special type in the bill as it is sent to the Commons; and then the Commons, if they see no objection, reinsert the excepted financial clauses. Or, the Lords leave the financial clauses in the bill, and follow them with a formal clause negativing the imposition of a charge, in the style of the recommendation "Don't put his head under the pump!" The Commons, if they please, then strike out the formal negative, and under goes the taxpayer's head.

## The Crown's Initiative

It is for the House of Commons alone to grant money and to limit the uses of its grant: it is for the House of Lords to assent to the grant, with the

by him that it is a money bill. Before giving his certificate, the Speaker shall consult, if practicable, two members to be appointed from the Chairmen's panel at the beginning of each session by the Committee of Selection."

limited power of criticism left to it by the Parliament Act. The whole initiative is with the Commons, but in the exercise of that right the House of Commons has imposed upon itself a very important limitation. By a self-denying ordinance it has deprived the generality of its own members of the power of initiative in imposing charges on the people, and has limited that power to the Crown. By the Crown, since ours is a constitutional and limited monarchy, we understand the King's executive ministers who sit in Parliament and are responsible to it. So the limitation of initiative by the House to the Crown is in fact a limitation to those of its own members who are responsible for the executive government. No grant can be proposed unless a minister demands it. No proposal can be made that a tax be imposed or increased unless a minister signifies the assent of the Crown to the proceeding, and thus certifies that the money is needed for the public service. No member not a responsible minister can get up and propose the imposition of a public charge on his own initiative. The matter is regulated by a Standing Order of the House of Commons. It is Number 66 which provides that "this House will receive no petition for any sum relating to the public service, or proceed upon any motion for a grant or charge upon the public revenue, whether payable out of the consolidated fund or out of money to be provided by Parliament,[1] unless recommended by the Crown."

[1] The words: "Or out of money to be provided by Parliament" had to be added to the Order, because of a growing practice of evading its spirit by moving a motion in such conditional terms. The limitation of initiative needs to be maintained with some jealousy. Owing to the accumulation of technical interpretations of the words of the Standing Order, its plain meaning is in danger from time to time of being whittled down.

The recommendation of the Crown may be communicated by a message under the sign manual, or by a formal verbal statement made in the House by a responsible minister; more commonly the recommendation is conveyed by a minister simply leaning forward in his place in the House, and touching a document with his finger as it is introduced.

The limitation of the financial initiative is sometimes spoken of as a prerogative of the Crown. The word is an unsuitable one. A prerogative is a privilege of the Crown that exists of its own force. The privilege or rather duty in question exists, not by its own force, not even by force of a statute, but by force of a mere domestic resolution of the House of Commons concerning its own procedure. A true prerogative right, such as that to make treaties, could not be affected by a resolution of the House of Commons. But by rescinding the Standing Order quoted above the House might to-morrow restore the right of initiative in taxation to the generality of its members. It is in its own wisdom that the House has established the rule, and the wisdom is beyond dispute. Limitation of financial initiative to the Executive is one of the sheet-anchors of good government. The balancing of revenue and expenditure is a nice and delicate operation; only the Executive can have the double knowledge needed for it, of what is needed on the one hand and of how much it will cost, and on the other hand of how much the taxes are likely to yield. It is the Executive which has sole responsibility for the national revenue and expenditure, and it is the Executive which should have control over them. Its plans once made must be rigidly adhered to; were the

balance of revenue and expenditure liable to be upset by any ill-informed, sudden, and comparatively irresponsible action on the part of a private member, the nation's finances must soon fall into wild disorder. It is easy to imagine the chaos which would result were a fervent patriot able to rise in his place and move the House, impromptu, to build ten fresh battleships "out of money to be provided." It is only too likely that in these days of high-strung emotions Parliament might be stampeded at times into some measure not much less reckless, which would necessitate at a moment's notice the immediate introduction of a fresh budget and the review of the whole taxation for the year. Against this we are protected by the necessity for a recommendation from the Crown as a condition precedent to any such proceeding.

There is another great mischief against which the limitation protects both the House of Commons and the taxpayer, one that was rife in the past before the limitation became so absolute as it is now: It protects them against the improper appropriation of public funds by members for the benefit of their constituencies. Formerly it was possible and common for the member for Looton, it might be, to move and carry the expenditure of £100,000 on a new harbour for his constituents. The present rule makes that impossible. All that a private member can do of his own initiative is to move a theoretical resolution that money might profitably be spent on such an object, which commits the House to nothing.

### FINANCIAL PROCEDURE IN THE COMMONS

It is then for the Crown, represented by its ministers, to demand such money as may be needed for the public service, for the Commons to grant it, and for the Lords to assent to the grant.[1] Provided with this clue, we may enter without dismay the maze of parliamentary procedure in matters of finance. We shall have a devious path to tread. In the House of Commons, financial procedure is planned upon no orderly or scientific scheme. It has been evolved bit by bit to suit the conditions and needs of the moment. Many of those needs are long since past, and many of the conditions are obsolete; but the procedure devised to suit them still remains, a meaningless ritual. Hence it comes that the rules of the House for financial business are full of fossils. Time much needed to do the work of the twentieth century is wasted on precautions against dangers passed with the seventeenth. The meaning and utility of much of the ritual is now no greater than that of the annual search for gunpowder in the cellarage. For this there is one change in the course of our history that is chiefly responsible. The years during which the procedure was being worked out were the years of the struggle between the Legislature on the one hand and the Crown on the other. The chief care of the Commons was at first to prevent the Crown from getting money except through Parliament, and in later days to prevent it from spending money on purposes other than those for which Parliament had provided it. Their procedure was planned to act

[1] Erskine May.

as a check on the Crown in the interests of themselves, the economisers. But times have changed. The rule of Parliament is established, and the power of the Crown is gone. A check upon the Executive's power over the purse is still needed by the Commons as much as ever, but the Executive upon whose power the check has to be exercised is now not the Crown but its ministers responsible to Parliament. Procedure planned to check the Crown is out of date. It is a beautiful structure, well worthy of a place in any museum; but it scarcely deserves the elaborate attention and praise which it still receives, because for any practical purpose in enforcing economy under modern conditions it is misdirected. What we need in our financial organisation in the twentieth century is that the House of Commons should direct its attention to imposing checks upon the extravagance of itself and its own ministers, and it is vain to allow an undue veneration for the sacred principles of the constitution to conceal that from us. Effective checks are needed even more under the present state of affairs than under that which saw the growth of the present system in Parliament. When the Executive was not responsible to Parliament, there was a natural antagonism between the two which stimulated the Commons to act as keen watch-dogs of economy, to guard the people's purse against undue exactions and against waste. There was the healthy parallelism and the division of interests between spenders and economisers which we have already noticed as one of the finest preventatives of extravagance. By the reduction of the Executive to complete dependence on Parliament that parallelism has been removed. There is no longer any antagonism to keep the Commons

on the alert, and they have drifted into becoming themselves the great spendthrifts. It results that much of what is of most historical interest in the procedure of the Commons is now of least practical value; much that was not necessary while the House was struggling to control the expenditure of the Crown, now that the House is itself the motive force in spending, is much needed, and is left undone. Obvious examples of these imperfections will exhibit themselves unmistakably in the course both of this and of the following chapters.

The whole structure of the nation's financial system is not dealt with by Parliament every year. That structure has two chief parts, revenue and expenditure. Of these Parliament authorises annually the whole of expenditure with a few exceptions. The whole of the revenue system with a few exceptions is authorised by permanent statutes which need no annual renewal. That those revenues are established by permanent statutes in no wise removes them from the control of Parliament. It is open to Parliament to repeal any of the statutes whenever it pleases. That part of expenditure which needs the annual and recurring authorisation of Parliament is called expenditure on Supply Services, and the process of its authorisation is called Supply. It includes expenditure on the Army, Navy, and Civil Services. That part of expenditure which is established by permanent statutes is called expenditure on Consolidated Fund Services. It includes the charges of the National Debt, payments to Local Taxation Accounts, the King's Civil List, and a number of special salaries, annuities, and pensions including part of the expenses of the Courts of Justice.

Taxes imposed by permanent statutes includ

all the principal headings of death duties, stamp duties, customs and excise, and so on. The exceptions which are reserved for annual authorisation are the income tax and the tea duty. One big direct and one big indirect tax are thus kept within the more immediate control of the Commons; and their importance is so great in the annual scheme of revenue that by controlling them the House controls in practice the whole finances of the year. By refusing to authorise them it could paralyse the Executive. A good reason for the selection of these two taxes in particular is that they are the most variable; changes are made in them more often than in others. Yet the other taxes are not out of the control of the House. At any time it may change or repeal the permanent statutes by which they are established, and not seldom it does. There is another means by which it can exercise direct control over the whole revenue of the year. Amongst the supply services voted annually are the expenses of the departments which collect the revenue. By refusing to vote them the House could bring those departments to a standstill and prevent the Executive from collecting any revenue, even that authorised by permanent statutes.

The annual and recurring financial business of the House consists then of the authorisation of expenditure on supply services, and of the reimposition of the income tax and the tea duty. At the very beginning of the annual session the ball is set rolling. It is for the Crown as the head of the executive power to demand money for the needs of the nation, and this it does in general terms in the speech from the throne, which is delivered as soon as ever the House meets. After the usual observations about

the state of Europe, which are addressed to both Houses, the ministers, speaking with His Majesty's voice and in his name, inform the House of Commons that the estimates for the expenditure of the coming year will be laid before them in due course. His loyal Commons address the King in reply with their humble thanks, and so the business begins. The House is now started on its double task of deciding upon the expenditure of the year and of providing funds to meet the expenditure upon which it has decided. All expenditure, as we have seen, has to be proposed by or with the consent of the Executive. A proposal for expenditure comes to the House in the form of an estimate, which is presented by the minister responsible for the department by which the money included in the estimate is to be spent. The manner in which the House receives and discusses the estimate or any other proposal for expenditure is governed in the first place by certain Standing Orders, Nos. 67 and 69, which provide that the House "will not proceed upon any petition, motion, or bill for granting any money . . . but in a committee of the whole House"; and that the House "will not proceed upon any motion for an address to the Crown, praying that any money may be issued or that any expense may be incurred, but in a committee of the whole House." The best reason for the Orders is that they give the House time to realise what it is about whilst it is getting into committee, and so save it from being taken by surprise by sudden proposals for expenditure. Another precaution which the House has adopted for the same purpose, to guard itself against surprise, is now the subject of Standing Order No. 71, which provides that "if any motion be made in the House

for any aid, grant, or charge upon the public revenue, whether payable out of the consolidated fund or out of moneys to be provided by Parliament, or for any charge upon the people, the consideration and debate thereof shall not be presently entered upon, but shall be adjourned" to a future day, in short, and then referred to a committee of the whole House before any resolution or vote is passed. So whenever expenditure is proposed it has to be adjourned at least once and then to be considered in committee.

## Committee of Supply

After the King's speech has started the session, the first step in financial business is the introduction of the estimates, which are the executive's demands for authority to spend the sums specified therein on the specified purposes. Suppose that the House has met in February. Then there will be presented to it within the first fortnight or so the Army, Navy, Air Force, and Civil Service Estimates for the financial year which will begin on the next first of April, with a memorandum explanatory of each from the responsible minister, and a statement of the variations on the estimate for the current year.[1] For the Civil Service Estimates the minister responsible is the Financial Secretary to the Treasury; for the Naval and Military Estimates it is the First Lord of the Admiralty and the Secretary of State for War

[1] It is to be observed that the comparison in these estimates is with the sums granted in the ordinary estimates for the preceding year, not including sums granted in Supplementary Estimates, which have not been passed by the House at the time at which these estimates are prepared.

respectively. In the meantime the House has taken an important formal step. Estimates according to the rule can only be considered in committee; so immediately after the address in reply to the gracious speech the House has resolved that on a given day it will resolve itself into committee to consider the Supply to be granted to His Majesty, and has ordered that the estimates presented be referred to the committee. Thus is the committee brought into existence in which practically the whole of the financial business of the session will be transacted.

The Committee of Supply is a committee of the whole House, which means that it is the House of Commons under another name. It is presided over by a chairman instead of the Speaker, and members are set free happily to talk as often as they like upon a motion, instead of only once as at other times. Otherwise there is no material difference between the House as House and the House as Committee of Supply. When the day comes round on which the House has resolved that it will go into Committee of Supply to consider, it may be, the Army estimates, a motion is made "that Mr. Speaker do now leave the chair." This, the means by which the House gets itself into committee, at once runs the financial business out of its forward course and aground on another fossil embedded in procedure. It is one of the sacred principles of the constitution that grievances precede Supply. Before money is granted to the Crown, the Crown must listen to its subjects' complaints and promise them their *quid pro quo*. The rule, vital in the sixteenth century, is meaningless now that Parliament holds the remedy for grievances in its own hand. It serves merely to provide an

occasion for a debate of a general character on some question of topical interest.

Members ballot for precedence for their motions on this occasion. Only one vote is taken on the debate: if the mover of the first motion does not divide the House, then the next motion in order of the ballot can be considered; but a division ends the discussion, and the Speaker leaves the chair. The subject-matter of the "grievance" motion must have some relevancy to the estimates to be considered. Thus the debate covers some of the ground which must be covered afterwards in committee; and its utility, now that its constitutional purpose no longer exists, is very questionable. The best thing that can be said for it is that it gives a private member one of his few chances of raising a subject and of bringing a minister to book over an abuse, since the choice of subject depends on the ballot and not on the whips. In any case not so much time is now spent on these debates as of old. Grievances no longer precede Supply whenever the House goes into Committee of Supply. The debates are limited by the Standing Orders to the four occasions on which the Speaker is first moved out of the chair for the committee on the Navy, Army, Air, and Civil Service estimates respectively. With the "grievance" debate safely ended, the House is in committee and the financial business of the year is under-way.

When the Committee of Supply sits for the first time to consider either the Navy, Air, or Army estimates, a general statement is made by the responsible minister on the whole of the estimate, and a full-dress debate is held thereof. We have already, in the last chapter, considered in some detail the

form of the estimates presented to the Committee. It is enough here to remind ourselves that they are divided into Votes, each of which specifies a service and the sum of money to be spent upon it. *These are put to the Committee, Vote by Vote, in* the form of such a motion as "that a sum not exceeding £—— be granted to His Majesty to defray the expense of such and such a service, which will come in course of payment during—(the next financial year)." These motions the House discusses and the dissatisfied move amendments. No private member, it will be observed, can of his own initiative move an increase in a Vote; that would require a recommendation from the Crown. If the House desires to increase a Vote, the original estimate must be withdrawn, and a revised estimate introduced by a Minister. But a private member may move the reduction of a Vote, for such a motion imposes no charge on the public, and that is in fact the only form of amendment that can be made. Any member indeed may move the reduction of any charge, tax, or proposed expenditure. A motion of the sort need not be made in Committee, because the need for the preliminary committee stage applies, according to the Standing Orders, to the issuing of money or the incurring of taxation only; it applies, that is, only to the increases of charges on the public, not to their diminution.

The Committee of Supply can vote the grant proposed to it, or refuse it, or reduce it. It cannot annex a condition or alter the destination of a grant, because that might be to propose in substance a new grant. When it has acted as seems best to it within those limits, the Chairman reports to the Speaker the progress which has been made,

and it is ordered that the report be received on a future day and, to keep the Committee alive, that it have leave to sit again. That future day having come, probably after several adjournments, a motion is made that the House doth agree with the Committee in the resolution to which it has come. This is the Report stage, on which the whole matter can be debated over again, when members have forgotten most of what took place in Committee. Finally, after that second debate, the House in due course agrees with the Committee's resolution, and so the work of the Committee is perfected. Thus the House as House has to rediscuss and approve the resolutions which it has itself made as Committee. Certainly the process secures ample formality in the high matter of the authorisation of expenditure: whether it be not too ample there may be some reason to doubt.

It is to be observed that the sum voted in Committee of Supply for each Vote of the Estimates is a net sum: it is the gross sum required for the service of the Vote, less the sum to be appropriated in aid of that service out of the minor receipts of the department, as specified in the estimate. The distinction is of some importance. According to a ruling of the Speaker, a member may not in supply move the reduction of an Appropriation in Aid. Any good reason for this state of affairs it is difficult to see, when a member may move the reduction of the grant itself; but so it is. The effect of the rule is wholly to remove the gross sum estimated for a Vote from the control of Parliament. All that Parliament controls is the net expenditure. Legally the rule is based upon the wording of the Public Accounts and Charges Act of 1891, by which the system of appropriations in aid was established.

According to the wording of the Act it is for the Treasury to appropriate the receipts in aid of the votes, and that is considered to remove the matter from the sphere of influence of the Committee. Such a result, it may be suspected, was never contemplated when the Act was passed.

Appropriations in Aid may be a small affair in practice, but in theory the inability of the Committee of Supply to deal with them makes a breach in the rotundity of its control of finance. There is much to be said for their abolition and for the payment of all sums so received straight into the Exchequer Account in the same manner as a part of them is now. It would close a breach in the Commons' defences: it would do away with an exception to the admirable rule that all receipts are to be paid into a single account, the Exchequer Account, and to be paid out only under authority of Parliament. It would thus promote simplicity, both in the form of estimates and in that of accounts. Against this it is commonly argued that to pay the receipts in question into the Exchequer Account and out again would swell the apparent revenue and expenditure for the year by cross entries of an artificial sort, and so give a false idea of the nation's actual incomings and outgoings. It is not easy to see the force of this argument. Minor receipts of the departments are as much revenue as the big collections of the Revenue Departments proper. It is true that they are not strictly speaking taxes, although a great part of them are fees, which are much the same thing. No doubt it is desirable that the taxpayer should be able to see at a glance in the annual accounts just how much he is paying in taxes; but that purpose would be adequately served

by a footnote to the annual Exchequer Account, stating the deduction to be made from the total receipts on account of minor receipts by the departments not in the nature of taxation. It is also argued that, unless allowed to appropriate their minor receipts in aid of their expenses, the departments would have no inducement to realise them. But the great revenue departments have no such inducement to be diligent in the collection of revenue, and nobody suggests that, lacking it, they neglect their duties. The contention merely underrates the efficiency of the Civil Service. To the external critic the arguments against appropriation in aid must seem to have the best of it: to the minds of those engaged upon the work of administration there must appear great advantages in a system which leaves these sums in the hands of the departments and at their disposal.

Such is the history of a single Vote in Committee of Supply. There are some 150 Votes in the estimates to go through the process, so that an alert Opposition has plenty of scope for its activities. It is the object of the Opposition in the party game to see that the Government makes as little progress as possible with its legislative programme, and a good way to hinder it is to spend as much time as possible on the routine financial business of the session. Were unlimited discussion of every Vote to be allowed, an obstructive Opposition could take up the whole session very contentedly with Supply. To prevent that the time to be spent upon Supply[1] is limited by the rules of the House

[1] Including Votes on Account and procedure in Committee of Ways and Means and on Reports, but not including "grievance" debates and supplementary estimates.

to twenty days. For eighteen days the House may discuss away, but the nineteenth is a day of judgment. On that day all outstanding votes have to be passed in Committee. On the twentieth day all remaining Report stages have to be worked off. However little progress has been made in the eighteen days, on the nineteenth the matter must be brought to a conclusion. In practice the employment of the allotted days is not left altogether to chance. The whips arrange that certain votes shall be selected for discussion which will give each party an opportunity to raise matters of special interest to it. If matters of special importance turn up in the course of the Session which can best be discussed in Committee of Supply, the Ministry can increase the number of allotted days by three. Under modern conditions small progress is commonly made with the detailed consideration of the estimates before the axe falls on the last day but one of the allotted days. Between a third and a half of the total expenditure for the year is often voted then in an hour or so, without any sort or kind of debate or criticism. A more unsatisfactory state of affairs could hardly be imagined. It reduces the whole laborious process of the control of expenditure by the House to something of a farce. In particular the elaborate arrangement for the reconsideration of every vote on Report is exhibited as mere waste of time. It is obviously absurd to consider some votes twice over, when so many are not discussed at all. The time spent upon the Report stages of Supply resolutions (which is not, however, much) might well be saved for the discussion of one or two of those Votes which are now passed undiscussed under the closure; and the same may be

said of much of the time spent on other formal business in connection with finance which remains to be described.

## The Committee of Ways and Means

In the Committee of Supply the House considers a part of the programme of expenditure for the following year and authorises it all. But it has not discharged thereby the whole of its financial functions. It has decided that the sums asked for shall be granted, but it has not decided how they are to be provided. There is, indeed, only one way in which they can be provided, and that is by issuing them out of the Consolidated Fund, which is the fund into which the whole public revenue is paid; so that the distinction may seem a subtle one. But it is important enough, according to the procedure of Parliament, to necessitate a distinct and parallel series of resolutions. They are dealt with in another committee, the Committee of Ways and Means, which is the House under yet another name. At the same time as the Committee of Supply is originated, immediately after the Gracious Speech, and in the same way, the Committee of Ways and Means is brought into being "for raising the Supply to be granted to His Majesty," and thereafter its procedure in the whole elaborate process of renewals and Report stages is the same. The work of the Committee is to provide money to meet the grants which have been authorised. The Committee of Supply is concerned with expenditure; this other committee is concerned with revenue. Its first business, and its only real business,

to twenty days. For eighteen days the House may discuss away, but the nineteenth is a day of judgment. On that day all outstanding votes have to be passed in Committee. On the twentieth day all remaining Report stages have to be worked off. However little progress has been made in the eighteen days, on the nineteenth the matter must be brought to a conclusion. In practice the employment of the allotted days is not left altogether to chance. The whips arrange that certain votes shall be selected for discussion which will give each party an opportunity to raise matters of special interest to it. If matters of special importance turn up in the course of the Session which can best be discussed in Committee of Supply, the Ministry can increase the number of allotted days by three. Under modern conditions small progress is commonly made with the detailed consideration of the estimates before the axe falls on the last day but one of the allotted days. Between a third and a half of the total expenditure for the year is often voted then in an hour or so, without any sort or kind of debate or criticism. A more unsatisfactory state of affairs could hardly be imagined. It reduces the whole laborious process of the control of expenditure by the House to something of a farce. In particular the elaborate arrangement for the reconsideration of every vote on Report is exhibited as mere waste of time. It is obviously absurd to consider some votes twice over, when so many are not discussed at all. The time spent upon the Report stages of Supply resolutions (which is not, however, much) might well be saved for the discussion of one or two of those Votes which are now passed undiscussed under the closure; and the same may be

of finance they have proposed." The liberty applies to questions of taxation only, not to questions of expenditure. A direct defeat of the Government in the Committee of Supply must involve its fall. The reason is clear: if the Government be refused leave to get money in one way, it can make some alternative proposals; but if it be refused leave to spend money on some service which, by the fact that it has proposed it, it has guaranteed to be essential, there is no alternative and the matter is irremediable.

As already mentioned, authority for collecting the greater part of the taxes is derived from permanent statutes and needs no annual re-enactment. The tea duty and income tax alone need that; so unless the Chancellor has increases, reductions, or alterations in permanent taxes to propose, when the Committee has heard and discussed his Budget statement in a full-dress debate about the burning questions of high financial policy, all it has to do is to re-enact the tea duty and income tax, and the revenue system for the coming year is then complete. Resolutions are proposed to it re-enacting them, and if any amendment is needed in the existing law of taxation that is also embodied in a resolution. It is the meeting of the Committee of Ways and Means to consider the first of these resolutions that, technically speaking, is the occasion of the Budget statement. The resolutions may be discussed and amendments moved, but a private member cannot propose an increase of taxation or move an amendment that would have the effect of upsetting the whole balance of the year's finance. When the Committee of Ways and Means has dealt with the resolutions and they have been reported, its practical work is finished.

But not its formal work. It is the function of the Committee not only to authorise such taxes as need authorisation but to say also how the credits granted in the Committee of Supply are to be met. To cover the Supply resolutions which grant sums to defray expenses in the ensuing year Ways and Means resolutions must be passed saying how those sums are to be provided. When the Committee of Supply has got the estimates voted, the House transforms itself into a Committee of Ways and Means and authorises the issue of money to meet the supply. The votes in the Committee of Supply have their echo in the Committee of Ways and Means, in the form of motions by a minister "that towards making good the supply granted to His Majesty for the service of the financial year, the sum of £—— [corresponding to the sums voted in Supply] be granted out of the Consolidated Fund of the United Kingdom."

The Consolidated Fund, as has been explained, is the fund into which the proceeds of all taxation must be paid. It is the Committee of Ways and Means that controls it, providing for its refreshment by new taxation and for its employment by the motions authorising issues therefrom.

The sums voted in the Committee must never exceed the sums previously voted in Supply, and therefore the final authorisation of the Ways and Means resolution in the Report stage must not precede the Report stage of any of the Supply resolutions on which it is based. Theoretically there may be discussion on the motions in the Committee of Ways and Means, and amendments may be moved to reduce the amount to be issued, but not to increase it, because that, as an increase

of the charges on the public, can come only from the Crown. Actually the proceedings are almost always purely formal. What then is the value of this step in financial procedure? Historical interest it may have, as a relic of the time when the House was concerned to put every possible check upon an independent Executive. Practical value, now that the responsibility of the Executive to Parliament is secured, it would seem to have none.

## The Appropriation Act

At the point at which we have arrived in the procedure of the House, the estimated expenditure has been approved in Committee of Supply, and re-approved on the Report of Supply, and approved a third time in Committee of Ways and Means, and a fourth time on the Report of Ways and Means, and yet it has still a long road to travel before it is out of the wood. So far it has received the approval of the House of Commons only; and the House of Commons, for all its exclusive privileges in matters of finance, cannot give a financial proposal the force of law by means of its own resolution alone. Every financial resolution of the House of Commons before it becomes law must be presented to the Lords for their assent and to the Crown; and for that purpose it must be embodied in a bill and pass through all the regular stages of first reading, second reading, committee, report if necessary, and third reading, both in the House of Commons and in the House of Lords, and lastly it must be presented for the Royal assent. Money bills the purpose of which is to give the force of law to financial resolutions of the House of Commons are based upon the

resolutions in Committee of Ways and Means. Since the Committee passes two sorts of resolutions there are two sorts of bills. There is first of all a bill based upon the resolutions re-imposing the tea duty and income tax. This is the Annual Finance Bill. This is passed through all its stages as soon as may be in the Session. It is the statutory basis for that part of the revenue system which needs annual re-enactment. Secondly there is a bill based upon the Ways and Means resolutions, which authorise the issue of sums out of the Consolidated Fund to meet the grants in Supply. This is called the Appropriation Bill,[1] and it is passed towards the end of the session, when all the business of the financial committees has been got through. It is the keystone of the financial arch. It gives statutory authority to the resolutions for the issue of money out of the Consolidated Fund, and it confers certain powers upon the Treasury to borrow in anticipation of revenue. But it does more. The Ways and Means resolutions are general: they authorise the issue in a lump sum of the amounts granted in Supply. The Appropriation Act takes the lump sum and splits it up as voted in Supply, appropriating the sum granted for each Vote of the estimates to the services of that Vote, and thus making it illegal to spend it on any of the services of any Vote other than that to which it is appropriated. Schedules are appended to the Act in which the Votes of the Estimates are set out in detail, with the sum granted for each and the amount of the minor sums to be received by the departments which may be appropriated in aid of the expenditure on each Vote, and it is enacted that "all sums granted by the Act as appears by

[1] Earlier Consolidated Fund bills are dealt with later.

the schedules are appropriated for the services and purposes therein expressed." The amount the expenditure of which is thus authorised and appropriated by the Bill must not of course exceed the total supply granted, and it is the business of the Speaker, acting through the Public Bill Office of the House of Commons, to see that it does not. The second reading of the Bill provides one of the rare opportunities still left to the House for a debate in which it is in order to raise practically any matter of administration in heaven or earth or the waters under the earth. When the Bill has received the Royal assent, the financial legislation of the year as far as Parliament is concerned is complete.

## Votes on Account.

The Parliamentary session begins in January or February: the financial year ends on March 31st; and owing to the long discussions of the estimates in Supply the Appropriation Bill, which makes operative the financial provision for the year, usually does not get passed until towards the end of the session in August. Now the only money at the disposal of the Executive in March is the money granted for the service of the year then current, which is limited to that service by the Appropriation Act of that year and cannot be used for the service of the next year. Were Parliament therefore to take no steps before March 31st, the executive would be left without power to spend a penny or to incur a pennyworth of liability on the services of the new financial year until such time as a fresh Appropriation Bill should receive the Royal assent,

an obvious impossibility. To fill up the gap in time provision adequate to meet the needs of the first part of the coming year has to be made by a special process before April 1st. In outline the process is a reproduction of the full process of financial legislation already described, and it puts at the disposal of the Executive money enough to go on with until the Appropriation Act is passed to legalise the whole provision for the year. In order to give time for all the various stages of procedure, a beginning has to be made with this process early in March. The first step is to get enough money voted in the Committee of Supply to meet the immediate needs in the coming year of each of the chief heads of service, Navy, Army, Air, and Civil Service. When they send their Estimates to the Treasury, the departments furnish information to it as to the amount which they will need to have granted to them to go on with before the end of the financial year. In the Parliamentary procedure for granting them what they need, there is a difference between the procedure in the case of the Civil Service Votes and that in the cases of the Navy and Air Votes. It affects the whole system on which the nation's accounts are kept, and it needs therefore careful description. As already observed, the Appropriation Act specifies the services included in the Estimates, Vote by Vote, and the sum granted for each, and then appropriates the sum to the service, so that it becomes illegal to use a sum for the service of any Vote other than that for which it was granted. That is the rule, and in the case of the Civil Service Votes it is an absolute rule; but in the case of the Navy and Air Votes (we shall come to the Army later) the exigencies of administration give rise to an

important exception. In contrast with the very heterogeneous character and distributed control of the Civil Service grants, there is a unity in the purpose for which these grants are made, and they are each subject to a single control. There is not therefore in their case the same reason, in the interests of order and simplicity in accounting, for keeping at all times an absolutely impermeable division between the sums granted for each Vote; and for convenience' sake it is useful that the Executive should be able to make temporary use of the money granted for one Vote in paying for the services of another. The Admiralty and the Air Ministry are accordingly allowed to make temporary use of money granted to them on any one of their Votes for any other Vote. Ultimately of course they must bring their expenditure into accordance with the provisions of the Appropriation Act, and in no case can they exceed the aggregate amount granted; but in order to put them in a position to carry on their work until the Appropriation Act is passed, thanks to this special liberty it is enough for them that one or two Votes should be passed before March 31st big enough to give them as much money as they will need for all their various purposes during the interval. It is customary for this purpose to take in the early part of March the Votes for pay for the Navy and Air Force and if necessary one or two others, which provide enough money for the purpose.

We have seen that there is now only one Army Vote (besides Vote A which is not a money Vote, but a means of obtaining Parliamentary approval for the numbers of men serving). The Army practice, therefore, which was formerly identical with that

described above, is now to take a Vote on Account, as is done for the Civil Votes.[1]

In the case of the Civil Service Votes there is no such liberty to make temporary use of money granted for one Vote for the service of another. The consequence is that an estimate has to be presented early in the session by the Financial Secretary to the Treasury of the amount required to be voted on account of each of the Civil Service Votes before March 31st, in order to enable the business of civil government to be carried on in the coming year until the passage of the Appropriation Act. The preparation of this estimate is governed by a rule that a vote on account must be restricted to such services as have already received the sanction of Parliament. In this hasty business of making temporary provision for the beginning of the coming year, the House must not be called upon to give its assent to anything new. Having received the estimate, the Committee of Supply passes a resolution granting the amounts asked for therein. Its Vote on Account for the Civil Service is in the same form as its ordinary resolutions: it specifies the total grant, and the distribution of the total amongst the departments is set out in a schedule.

The Supply Resolutions dealing with the Civil Service and Army Votes on Account, and the Navy and Air Force Pay Votes, safely passed, the further procedure of financial business already described is run through in respect of those resolutions, often in a desperate hurry to get it done before the financial

[1] There is nothing to prevent the Navy or Air Force from taking a Vote on Account, if for any special reason this is preferable; and the Admiralty did this in 1922–23 when the preparation of their detailed Estimates was unavoidably delayed by the Washington Conference and the Geddes Committee.

year runs out. The Supply Resolutions are reported. The Committee of Ways and Means meets and authorises the issue from the Consolidated Fund of the amounts granted in Supply. A Bill is at once introduced, based upon the Ways and Means resolution. This is called the Consolidated Fund Bill. Its operative clause enacts that the Treasury may issue out of the Consolidated Fund the lump sum voted and apply it towards making good the supply granted to His Majesty for the service of the ensuing financial year. Except for powers to the Treasury to borrow in anticipation of revenue, that is all. The Bill is rushed through all its stages and usually receives the Royal assent in the nick of time on the last day of March. That done, the Executive is in a position to face the new financial year, and the House to proceed at its leisure with the regular business of Supply. It should be observed that the Consolidated Fund Bill is not an Appropriation Bill: it does not distribute the sum granted amongst the particular Votes for which it was granted. The Treasury may issue any part of it for any supply granted, a circumstance which has interesting results to be considered hereafter. When the Appropriation Act is passed it covers all the grants included in the Consolidated Fund Act and appropriates them; but until then the grants are at large.

In his estimate for the Vote on Account of the Civil Service the Secretary of the Treasury specifies the length of time for which he has made provision. The House of Commons is supposed to guard with some jealousy against temporary provision of the sort being made for too long a period, because to refuse Supply is its final means of bringing to order an Executive with which it is in disagreement, and

once the Executive has got its Consolidated Fund Act passed it is independent of the House until the money voted therein is exhausted. At ordinary times, however, the House is wont nowadays to assent without demur to a provision for the expenses of four or five months, long enough to last until the Appropriation Act can be passed in the normal course. Formerly it used to insist on a shorter provision, and then it was sometimes necessary to pass a second Consolidated Fund Act, when the funds liberated by the first had all been used up before the Appropriation Bill could be carried. There is, however, one occasion on which the length of time for which provision is to be made is still a burning question, and that is when a Vote on Account and a Consolidated Fund Bill are needed to enable the Government to be carried on while the sittings of the House are interrupted by a dissolution and a general election. The Opposition will then see to it that the Government does not get money enough to enable it to postpone the evil hour when it must call the new House together and face, as they hope, a majority of its opponents.

## Supplementary Estimates

Did we live in a perfect world in which nothing unforeseen ever happened and everybody always did what they were told, the machinery as it has now been described would be all that was needed to get the financial work of the Legislature done, year by year. But the unforeseen does happen; emergencies arise, and it is seldom that the original estimates are found to meet all the needs of the

year for which they were intended to provide. It would be strange if they did, because they are prepared in October and November to meet the needs of a year which begins in the following April and so does not end until some fifteen months later than the time at which the estimates were settled. Some fresh need for expenditure, unforeseen and unprovided for in the estimates, may be expected to occur in the course of the fifteen months. When it does, to provide for it one or more Supplementary Estimates are introduced towards the end of the financial year, in February or March. An estimate of the sort is needed either when the amount granted in accordance with the original estimate for a service is found to be insufficient for it, or when a need arises for expenditure on some new service not contemplated in the original estimates. In form a Supplementary Estimate is similar to the original estimates already described, and to authorise the expenditure which it demands the same procedure is necessary. To regularise matters the authorisation must be complete before the end of the financial year in which the expenditure was incurred; and that is why the receipt of supplementary estimates for the current financial year and their consideration in Committee of Supply is always one of the first concerns of the House of Commons when it meets for the new session in January or February. About the same time that the first Navy and Air Votes, which are the Votes for pay, and the Vote on Account for the coming year are passing through Committee of Supply, that committee is also meeting to vote the Supplementary Estimates for the current year. They pass through all the formal stages of Committee and Report, both of Supply and of Ways

and Means. The sums voted for them are usually included in the same Ways and Means resolutions as those which cover the Vote on Account and Navy and Air Force Pay Votes and serve as a basis for the Consolidated Fund Act; and it is that Act which clothes the grants for the Supplementary Estimates with statutory authority. It does not appropriate them, any more than it appropriates any other grants. That is done by the Appropriation Act which is passed, as we have seen, towards the end of the session. When the House holds an Autumn Session it is sometimes able to get through a good deal of work on the Supplementary Estimates then. The Ministry is glad to do so, because it is a decided hindrance to its work that when the House meets, vigorous and refreshed after Christmas, its enthusiasm should have time to cool while it is getting through routine financial work under pressure of the approaching end of the financial year.

Because of the long forecast that has to be made in preparing the estimates, Supplementary Estimates may often be a necessity, but they are always a necessary evil. The House and the taxpayer have the right to expect that the estimates and the scheme of the Budget shall be rigidly adhered to by those who have to administer them. Public control of public expenditure depends for its efficiency in large measure on the financial scheme for the year being presented to the House and considered and approved once and for all and as a whole. To allow the scheme, once approved, to be treated as something still fluid and liable to extensive modifications must infinitely weaken effective control, and Supplementary Estimates are the most harmful way of doing so. To make anything but the most

restricted use of them must deprive the whole system of Supply of its meaning and utility. Whilst admitting therefore that they are occasionally necessary in the case of emergencies unforeseen and unforeseeable, we should remember that they are always harmful. They are a diseased excrescence on the year's finance, and the success in finance of the Ministry may be measured by their ability to do without them. As a rule no provision for supplementaries is made in the Budget, because it is hoped to finance them out of savings.

## Votes of Credit

The procedure by Supplementary Estimates covers all ordinary emergencies; but extraordinary and critical emergencies may arise for which that procedure would be too slow. Suppose that the nation is threatened with war; the Executive will then require a large sum in a hurry, and will not be able to say in detail how the sum is to be applied. The recognised procedure under such exceptional circumstances is for the Executive to ask the House for a big sum on a vote called a Vote of Credit, specifying in an estimate expressed in quite general terms the manner in which it is to be spent. Like all other resolutions involving expenditure the vote must be considered in a committee of the whole House and confirmed by the next regular Consolidated Fund Bill or by a special one. The House in Committee grants a sum in gross to the Executive, to which it leaves the responsibility of distributing the money. Needless to say, no part of the sum so voted must be used except for the purposes for

which it was voted; it must not be used to fill up deficiencies in the ordinary votes. It is for expenditure in war time that this form of procedure has been most used in the past.

### The Estimates Committee

Such is the regular machinery by which Parliament discharges its financial functions year by year, and all the processes described hitherto are necessary to the financial legislation of the year. In addition to its legislative business, the House of Commons has lately undertaken a further financial activity which is not essential to its work of financial legislation, however useful it may be. Dissatisfied with its control of the estimates, as it well may be, it has appointed year by year a Select Committee of some fifteen members to examine and criticise the estimates in greater detail than is possible in the Committee of Supply. The work of the Committee is to consider what ends the spenders are proposing to themselves, and then to see that the means which they propose are the best possible to secure those ends. According to the terms of its Order of Reference, the Committee is appointed "to examine such of the Estimates presented to the House as may seem fit to the Committee, and to report what, if any, economies *consistent with the policy implied in these Estimates* may be effected therein." Unlike the Budget or Estimates Committee of continental parliaments, and in particular that of the French, this committee is a purely advisory body: it has no responsibility for the estimates which it examines. It cannot reject or approve any estimate, nor can

the minister in charge of any estimate be condemned by its adverse decision or relieved of his own responsibility by its approval. Its functions are those of a critic and scrutineer of details. In practice it takes a single estimate or group of estimates, such as the Navy Estimates, and sitting with a Treasury Official ever present at its deliberations it examines them item by item, seeking to detect extravagances, reduplicated or obsolete charges, and all other offences against economy. There is a consensus that as an instrument of economy the Committee has not justified all of the high hopes that were held for it at its first appointment.

There are various other exceptional methods, survivals and anomalies for the most part, in the financial procedure of Parliament, some of which have still some use; but they are not essential to Parliament's regular financial work, and we need not allow them to delay us here. The methods described are those by which, year in and year out, Parliament decides what money is to be spent in the course of the year, and how that money is to be raised. The permanent acts imposing taxation together with the annual Finance Act and the Appropriation Act are the final authorities under which the taxpayer's pounds are removed from his pocket and paid over to the creditors of the state. Having considered them, we have finished for the present with the Legislature, and we can pass to the consideration of the work of the Executive acting under its statutory authorities derived from Parliament in the manner which has been described.

# CHAPTER IV

## COLLECTING THE REVENUE

The Executive receives from Parliament its power to act, in the manner described in the last chapter. The greater part of the taxes it is authorised to collect under permanent statutes. For the collection of income tax and tea duty it receives each year an authority which applies to that year only. Even in their case the basis of assessment and the manner of collection are governed by permanent statutes. The skeleton of the tax is permanent; all that the annual Finance Act does is to give it life for another year. It is essential that the Executive should be able to collect the tea duty and any fresh duties of customs or excise or any increases in old ones as soon as it is made known that they are to be imposed. Were it not able to do so, importers and manufacturers would scramble to rush dutiable goods into the country and to clear their stocks in the interval before the new or higher duties became operative, and the revenue would suffer. Thus it would largely defeat the purpose of any change had the Executive to wait to impose the new rates and charges until all the formalities could be fulfilled which are needed to make the Finance Bill law. For that reason it is customary for the Committee of Ways and Means to pass the resolutions imposing the income tax and tea duty,

and any new or increased duties, on the same day as they are announced in the Chancellor's Budget speech; and there was formerly a custom or tradition according to which the Executive thereupon at once exacted them from those upon whom they were imposed, trusting to the passing of the Finance Act to regularise the matter in due course. The custom was upset or destroyed by a decision of the courts in the case of Bowles *v.* Bank of England, part of the aftermath of the rejection of the Finance Bill of 1909 by the Lords. In that case it was decided that, custom or no custom, there was no legal authority to exact income tax until the resolution of the Committee of Ways and Means had been clothed by the Finance Act with the force of law. To put matters back on the old footing it was necessary to pass a special Act of Parliament, the Provisional Collection of Taxes Act of 1913, by which it is enacted that where a resolution is passed by the Committee of Ways and Means providing for the variation of any existing tax or for the renewal of any tax in force, and the resolution contains a declaration that it is expedient in the public interest that the resolution should have statutory effect, the resolution shall for a limited period have statutory effect as if contained in an Act of Parliament, and where the resolution provides for the renewal of a tax all enactments which were in force with reference to the tax as last imposed by Act of Parliament shall during the said period have full force. It is provided that the resolution shall cease to have statutory effect if not agreed to on Report within ten sitting days after the resolution was passed by the Committee. The confirming Bill must be read a second time within twenty sitting days of the passage of the

resolution, and the statutory effect of the resolution is to expire in any case after four months. This Act applies to duties of customs and excise and to income tax only.

As soon as the Committee of Ways and Means has passed its taxing resolutions, the Executive is fully armed by this Act with all the powers which it needs to collect the revenue. There is no interval in which manufacturers and importers can forestall any new charges, unless it be the hour or two between their announcement by the Chancellor of the Exchequer and the passing of the resolutions by the Committee.

The work of collection is done by the Board of Customs and Excise and the Board of Inland Revenue. To give a detailed account of the manner of collection of every tax and duty and of every other source of revenue would lead us too far into a field of unnecessary detail. It will be enough for our purpose to consider the methods by which two typical classes of revenue are gathered in: one indirect, the duties of customs and excise; and one direct, the income tax.

In early days, the King's taxes were received in gold and silver. The sheriff collected the coin and carted it to the King's Exchequer, where it was put into a chest. When the payments had to be made, it was with coin from the chest. In these days of banks, the process of collection is more refined. Payments nowadays, needless to say, are made in the vast majority of cases not in coin but in the convenient paper currency of cheques which the banks make it their business to supply. We have to bear in mind, throughout what follows, that in speaking of payments and remittances we

are speaking, not of the transfer of sovereigns from hand to hand, but of the transfer of credit from bank to bank by means of bits of paper.

At this point it will be useful, too, to pause and to point out a distinction which will help us in steering a straight course through the intricacies of the nation's accounts. It is the distinction between a balance and an account. Suppose that I have, in the common phrase, some money at the bank. What I have is not of course some coin in a box there. I have a right to call upon my bank, a solvent debtor of large means, for a certain sum. The sum for which I have the right to call upon it is my balance there. If I have the right to call for it in cash at a moment's notice, I call it a cash balance. Now that balance is the difference between the sums which I have paid into the bank and the sums which I have drawn out of it; and the record of all those transactions is my account. A balance is money or credit as good as money; an account is a record, and that is the distinction which it is useful to bear in mind. A single balance of credit may figure in many different accounts. There is unfortunately a source of confusion in the use of the word "fund," which is commonly used indifferently to mean either an account or a balance.

In primitive times men kept their money in coin, put away in boxes, and so did the state. Now we keep it in the form of a balance at the bank, and so does the state also. Just as the average man of means has an account with his bank, the credit balance of which is the money which he has, so the state has an account with the Bank of England, and the credit balance of that account is its available money. Its account there is called the Exchequer

Account, as already mentioned. The most important fact about it is that it is one and not many. Formerly different heads of revenue were paid into different accounts. By the Exchequer and Audit Act of 1866, which completed a long process of consolidation, all the different accounts were combined into this one, which is also called the Consolidated Fund. Sections 10 and 11 of the Act are as follows: "The Commissioners of Customs, the Commissioners of Inland Revenue, and the Postmaster-General shall, after Deduction of the Payments for Drawbacks, Bounties of the Nature of Drawbacks, Repayments, and Discounts, cause the gross Revenues of their respective Departments to be paid, at such Times and under such Regulations as the Treasury may from Time to Time prescribe, to Accounts to be entituled 'The Account of Her Majesty's Exchequer,' at the Bank of *England* and at the Bank of *Ireland* respectively, and all other Public Moneys payable to the Exchequer shall be paid to the same Accounts, and Accounts of all such Payments shall be rendered to the Comptroller and Auditor General daily, in such Form as the Treasury may prescribe: Provided always, that this Enactment shall not be construed to prevent the Collectors and Receivers of the said gross Revenues and Moneys from cashing, as heretofore, under the Authority of any Act or Regulation, Orders issued for Naval, Military, Revenue, Civil, or other Services, repayable to the Revenue Departments out of the Consolidated Fund or out of Moneys provided by Parliament (§ 10).

"All Moneys paid into the Bank of *England* and the Bank of *Ireland* on account of the Exchequer shall be considered by the Governor and Company of the said Banks respectively as forming One

general Fund in their Books; and all Orders directed by the Treasury to the said Banks for Issues out of Credits to be granted by the Comptroller and Auditor General, as hereinafter provided, for the Public Service, shall be satisfied out of such general Fund (§ 11)."

We shall see presently the effect of the Proviso to the first paragraph, and the meaning of some of the other clauses in these sections.

Roughly speaking then we may say that the Exchequer Account at the Bank of England is the state's one Revenue Account, and its balance on that account is the money which it has. After this short preface we are in trim to consider the system on which the money is collected.

Let us deal first with indirect taxation. A matter of interest is the men who do the work. The organisation of the central authority, the Board of Customs and Excise, has already been described. Ramifying from the Board at the Custom House there is a numerous local staff. The country is divided into districts and over each district there is a Collector of Customs and Excise. Under each Collector there are several Surveyors of Customs and Excise, and under each Surveyor there are a number of Officers, each of whom has his local station, and a number of Preventive-men. In the arrangement of their work there is that parallelism which we have already noticed as the secret of good administration in financial matters. For every officer who does the actual work of collecting, there is another who acts as a check upon him. This is brought about by a separation of the functions of assessment and collection. Take for example the collection of excise duties upon the whisky

*produced at a big distillery. If the distillery is big enough, it is made the permanent station of an* Excise Officer. The Officer communicates to the Surveyor of the district, who is his immediate superior, the amount of whisky sent out from the distillery. The Surveyor acts as assessing officer: he determines the amount of duty payable, and thereby "raises a charge" against the Collector of the district, who is his own immediate superior. Next he communicates his assessment to the Collector and to the central office, and it then becomes the duty of the Collector to collect the amount of the assessment. Thus assessment and collection are in different hands: should any evilly disposed person seek to defraud the revenue by corrupting its agents, he has not one official to deal with but two, and three if we count the Excise Officer.

Surveyors assess, and Collectors collect what Surveyors have assessed. The actual collection takes place as follows. The assessed person attends at the Collector's office to pay the duty. The Collector is legally entitled to demand cash; in practice small sums only are so paid. By arrangement the Collector agrees to take the payer's cheque: it must be either a bank cheque, which is a cheque that is drawn by the payer's bank itself under arrangement between them, or a cheque guaranteed by a bank. Having paid what he has collected into his local bank, the Collector remits it daily to the account of his Head Office at the Bank of England in Threadneedle Street. He also notifies his own head office daily of the amount which he has transmitted.

The Commissioners of Customs and Excise keep two accounts at the Bank of England: they are

*(1) the Account of the Commissioners of Customs and Excise and (2) the Account of the Accountant* and Comptroller General of Customs and Excise. It is to the former that the Bank credits daily all the sums received from the Board's Collectors; and it sends daily to the Commissioners a pass-book showing the state of the account. The sums collected are not left standing at the credit of that account. As we have seen, one of the fundamental principles of our system of national finance is that all revenue received is to be paid into a single account, the Account of H.M. Exchequer at the Bank of England, which also passes under the *alias* of the Consolidated Fund of the United Kingdom, and by the nick-name of the Exchequer for short. The Commissioners of Customs and Excise make daily transfers (of the available balance of revenue received) from their own account at the Bank of England to that general and central account. It has then passed out of their control into that of the Treasury. A cross-entry in the books of the Bank is all that is needed to make the transfer. They also transfer from time to time, and by a similar operation of cross-entries in the books at the Bank, a certain amount of credit from their own account to the account of their Accountant and Comptroller General. This last is a drawing account: it is the account upon which the Accountant General draws to meet the current expenses of the office, and for other purposes to be mentioned.

Reverting to the distinction between balances and accounts, we see that the credits collected are in the hands first of the local bank and then of the Bank of England. They are accounted for first in the Collector's local account, then in the account of

the Commissioners at the Bank, and finally, as to the bulk in the Exchequer Account at the Bank, as to a part in the drawing account of the Accountant General at the Bank. The process of collection involves two transfers of a balance only: from the taxpayer to the Collector's local bank and from the Collector's local bank to the Bank of England.

The organisation of the Inland Revenue is on similar lines. It has its local inspectors, the Inspectors of Taxes, each of whom is responsible for a Tax District, with a small staff of clerks, and, in the more important districts, with a junior Inspector or one or more Assistant Inspectors. The functions of the Inspector of Taxes are similar to those of the Surveyor of Customs: like him, he "raises a charge" against a Collector, who must account to the Accountant General of Inland Revenue and to an "Audit of Charge" staff at Somerset House for the amount charged against him. There is thus the same parallelism and division of functions in the collection of the direct taxes that we have already noticed in the collection of the indirect. The Collectors collect the direct taxes charged against them by the Inspectors of Taxes, and remit them to the account of the Commissioners of Inland Revenue at the Bank of England. Periodically the Commissioners of Inland Revenue transfer the proceeds of their collection from their own account at the Bank of England to the Exchequer Account.

The chief head of revenue with which the Board of Inland Revenue is concerned, the Income Tax, is collected on a system of its own. It is a cumbrous old machine, constructed when the taxpayer was less well broken to the bit than he is now. When the Income Tax was born, the taxpayer was

fearful of oppression at the hands of the local tax collector. Excise and excise man were still words as capable of raising a riot as they had been in Walpole's time. Dislike of inquisition into a man's means was strong then, and is not yet extinct. There are traces of all these things in the anomalies of the income tax machine, and of states of the social mind far more remote even than they. To protect the taxpayer from official inquisition, the collection of income tax is controlled by private persons not in the employment of the state. These are the District Commissioners of Inland Revenue, men of good standing in the district for which they act. If a taxpayer prefers to be dealt with by professionals rather than by amateurs, he may put himself into the hands of the Special Commissioners, civil servants of high standing appointed by the Treasury, who work in Kingsway. With the Income Tax, as with the taxes with which we have already dealt, assessment and collection are in different hands. To do the work of assessment Assessors are appointed by the District Commissioners. They are persons of repute in the district (which is commonly the parish), not Government servants, but in receipt of small fees. In theory they assess the taxpayer's income, and communicate the assessment to the Inspector of Taxes for the district. In practice the assessment is made by the Inspector on returns of income made by the taxpayers and transmitted to him by the District Commissioners, who have received them from their Assessors. In fact the amateur organisation of Commissioners and Assessors is of very little practical importance in comparison with the professional Inspectors; and the Royal Commission

on the Income Tax, 1920, recommended that th
office of Assessor should be abolished and that hi
duties should devolve upon the Inspector. Th
discontented assessee may complain to the Com-
missioners and ultimately to the High Court of
Justice.

So much for the assessment of the income tax now for its collection. To get in the money the District Commissioners nominate and the Board of Inland Revenue appoints Collectors in each parish or other district, who must be "able and sufficient residents." The local Assessor is often appointed Collector also, which is a departure from the good rule that collection and assessment should be in different hands. These Collectors are not Government servants, although they receive fees and commissions, but it was recommended by the Royal Commission on the Income Tax, 1920:—

(*a*) That all Collectors throughout the United Kingdom should be appointed by the Board of Inland Revenue;

(*b*) That the general management of the collection of the tax should be placed under the control of the Board of Inland Revenue, who are answerable for the revenue imposed;

(*c*) That in those areas in which it is convenient, and as soon as it is administratively possible, Collectors of Taxes should become whole-time Civil Servants.

The Collectors are nominally under the control of the District Commissioners, but practically under that of the professional Inspector of Taxes. They demand the amounts due for income taxes from the victims. When they have collected them, they proceed to transmit them to their central authority,

which is the Board of Inland Revenue. The Inspectors of Taxes also have an eye on the collection; they compare the Collectors' receipt books with their remittances, and inspect and report upon their schedules of arrears.

The administrative machinery of the Income Tax is very antiquated. It can only be made to work by a liberal disregard of obsolete statutory provisions, and it is much in need of modernisation.

There is a part of the detailed machinery provided by the statutes which govern the collection of Income Tax[1] which deserves mention, not for its practical importance, but for its curiosity. When our Governors in savage Africa impose a hut tax upon the natives, they are wont to assess them village by village, and to make the village as a community responsible for the whole amount assessed upon it. It saves the Governor trouble to do so, because it enables him to deal with the village headman as representative of the community instead of with each individual taxpayer. In the law for the collection of Income Tax there are the fossilised remains of a similar primitive system of taxation by village units. We find them in the provision that the Parish is liable, under certain circumstances, to make good defalcations by the local Collector and to make up revenue which he has failed to collect. This aged and outworn little piece of machinery links up the modern system of revenue collection with the Anglo-Saxon. Now the organisation of the state is strong and centralised, and the improvement of means of communication enables it to deal directly with each taxpayer. Then it was weak and distributed, and communications were difficult. The

[1] Taxes Management Act, 1880. § 79 (2) and ss. 112.

feeble state made no effort to deal with the individual taxpayer, but got the money out of the local authorities and left them to recover it from those ultimately liable. The history of taxation has been the history of change from that system to our present system of direct collection, and these fossils of the law of tax-collection link our present civilisation with that of 1500 years ago.

We have now dealt in some detail with the manner of collecting the indirect taxes, which are the duties of Customs and Excise, and the chief of the direct taxes, which is the Income Tax. Other revenue received by the two great revenue departments, the Boards of Customs and Excise and of Inland Revenue, is collected in the same way and is all ultimately paid into the Exchequer Account of the Bank of England. Revenue received by other departments is dealt with in the same way. Post Office revenues, the rents of Crown lands and revenue from other sources collected by the Woods and Forests, and the dividends from the nation's holding of Suez Canal shares, all are paid into the Exchequer Account. To that account are credited also the minor receipts of various departments, under the heading of Miscellaneous Revenue, including in particular the profits made by the Mint, which are principally derived from the coinage of silver. In accordance with the statutory rule that there must be only one central account to which all revenue is paid, as the amount of each of these minor contributions to the revenue is ascertained, it is credited to the Exchequer Account at the Bank of England. That is the rule, but it is a rule subject to several exceptions; and since the rule is also law, for each of the exceptions

there is or ought to be some legal authority. To complete the account of the system of revenue collection we must deal with the exceptions to the rule; with the cases, that is, in which revenue collected is not directly credited to the Exchequer Account but is diverted to some other purpose. They have some importance. It is upon the Exchequer Account, usually under its *alias* of the Consolidated Fund, that Parliament operates. Money paid into it is under the direct control of Parliament in its annual financial measures. Money not paid into it may escape that control. It matters, therefore, a great deal that when money is not paid into it there should be parliamentary authority for the proceeding and some provision for securing Parliament's control of the receipts, although under the circumstances the control can be exercised in an indirect manner only.

The first exception to the rule is an apparent exception only. Revenue collected for Customs and Excise is gross revenue. Out of it large allowances have to be made. When goods are exported on which excise duties have been paid, and when imported goods on which customs duties have been paid are re-exported, the amount of the duties is repaid in the form of rebates and drawbacks. Local collectors retain a part of the funds which they collect to make these repayments, and the Accountant General's drawing account provides the funds needed for payments of the sort at the Head Office. Thus the revenue for which the department has to account to the Consolidated Fund is net revenue: it is the gross revenue collected less rebates, drawbacks, and minor allowances. The Board of Inland Revenue deals

in the same way with the big allowances which are made annually to Income Tax payers. But even in a case in which the need for the interception of a part of the revenue is so obvious, express statutory authority is needed for the retention. In the case of drawbacks and rebates it is provided, as we have seen, by Section 10 of the Exchequer and Audit Act, quoted a few pages back.

The exception to the rule to be mentioned next is more substantial. The Boards of Customs and Excise and of Inland Revenue, before paying the revenue which they collect into the Exchequer Account, deduct enough to meet the expenses of collection, and keep it in their own hands. Their authority to do so comes from that Proviso to Section 10 of the Exchequer and Audit Act which has already been quoted. The manner in which the credit retained by the departments is accounted for is neat and even elegant. We may consider the case of the Board of Customs and Excise as an example. A Collector retains out of his daily receipts enough to meet the current expenses of his office, including salaries. What he retains remains in his hands as a cash balance at his local bank, for which he is responsible. He sends to the Board vouchers for the amounts retained. Similarly credits are periodically transferred from the Account of the Commissioners at the Bank of England to the drawing account of the Accountant General, to provide him with a cash balance on which to draw for the expenses and salaries of the Board in London. An account is kept by the Board of the total amounts thus retained for expenses out of the gross revenue collected, and once a month a claim is made upon the Treasury for credit in

*respect of them. Rough adjustments only are made in these monthly claims; but every quarter a careful adjustment is made, and at the end of* the financial year an adjustment as accurate as man can make it. Grants, be it noted, have already been voted by Parliament to meet the expenses of the department according to the Votes in the Estimates. When the Treasury receives a claim for credit from the Board, it makes sure that grants have actually been so made by Parliament to meet the expenses in respect of which the Board has retained money. It then makes a formal issue from the Exchequer Account to the account of the Board, and deducts the amount so issued from the credit voted by Parliament for the expenses of the Board, by debiting it to the account of the Votes of the Board kept by the Treasury. Having received the issue on to its account, the Board promptly pays it back into the Exchequer Account. Issue and repayment are no more than formal cross-entries in the books kept at the Bank, which serve to maintain the Exchequer Account as an accurate record of revenue and expenditure. The credit represented by these formal entries never, as we have seen, actually reaches the bank. It is retained and spent locally by the Officers of the Board.

In practice, for the sake of simplicity in accounting, the Board's daily deductions for expenses are dealt with as if they were all made out of Customs revenue, as distinguished from Excise revenue. The daily statements of the district Collectors show the amount of Customs and Excise revenue collected for the day. The total Excise revenue collected during the day is added up. This is credited daily, less the repayments, to the Exchequer Account

as Excise receipts. The balance is credited daily to the Exchequer Account as Customs Receipts: it is the Customs revenue collected during the day, less the amount retained for repayments and expenses. So, when the claim on the Treasury is made, it is made on behalf of the Customs revenue only, and one transfer only to the Exchequer Account as Customs receipts is all that is necessary, and not a double transfer to the Account for both Customs receipts and Excise receipts.

Receipts are also intercepted in this manner for several purposes other than the expenses of collection. Collectors in out-of-the-way localities are allowed to make use within their districts of their local balances for payments on behalf of departments other than their own, such as payments to local pensioners for the Admiralty and War Office, and for the Board of Trade. Vouchers for amounts thus advanced to other departments are sent to the Board of Customs and Excise in London. A claim is made by the Board upon the debtor department. That department, when it has verified the claim, notifies the Treasury; and the Treasury, by a book entry, writes the amount of the claim off the Votes Account of the debtor department, which records the amount of the money granted to it by Parliament for its expenses, and credits it to the Exchequer Account as Customs receipts.

It appears, then, that the revenue credited directly to the Exchequer Account by the Board of Customs and Excise equals the gross revenue collected, less drawbacks, rebates, and allowances, the expenses of the department, and local advances to other departments.

The purpose of the system of deductions is to

economise. For economy's sake, money is used where it comes to hand, without needless transfers of credit to and from London. Local payments are met out of local receipts, and accounts are adjusted by book-keeping entries. The system is simple and economical, but it involves leaving large cash balances in the hands of the Collectors. Wherever local officials are thus left with money under their control, good financial administration demands that there should be constant supervision as to the amount and the uses to which it is put. In this case the supervision is provided by a staff cf inspectors under the control of the Accountant and Comptroller General of Customs and Excise. They circulate amongst the Collectors, paying surprise visits to check their balances and accounts. It is arranged that every Collector shall be so visited at least once a year.

It was pointed out in the preceding chapter that one of the means by which Parliament controls the whole of the public finances of the year is through its power, when it is considering the estimates for the Revenue Departments in Supply, to refuse to vote the money needed for their expenses. In spite, it was said, of the fact that a large part of the revenue is collected under permanent statutes, Parliament can thus prevent the Executive from getting any revenue at all, by preventing it from applying any part of the Consolidated Fund to the payment, for instance, of its revenue collectors. It may be worth while to point out that the system described, under which the Revenue Departments intercept the sums needed for their expenses out of the revenue and do not pay them directly into the Consolidated Fund, in no way impairs that means

of control. For suppose that Parliament has made no grant for the expenses of the Revenue Departments, and suppose that the Board of Customs and Excise, for instance, retains nevertheless out of revenue collected sums to meet its expenses. Then, when it makes its monthly claim on the Treasury for credit in respect of the amount retained, the Treasury must answer, "We are sorry, but there are no grants of Parliament standing to your account out of which we can give you such a credit." Failing to obtain the credit the Board and its subordinates would be confronted with a deficiency in their accounts of revenue collected, and with the obligation to make it good out of their own pockets. Without the authority of the Parliamentary grant the Board must monthly make good what it has deducted for expenses: in short it must work for love or not at all.

The last exception to the rule that all revenue goes to the Consolidated Fund, or rather the last exception that can conveniently be dealt with here, is provided by the Department of Woods and Forests. As stated, it is net revenue only of the Crown lands and properties which that department pays to the Consolidated Fund, after deducting the cost of keeping up the estates and so on. It may be admitted that there are good reasons for the exception. The department has the ordinary business of land ownership to carry on, and it is convenient for it to enjoy a wide freedom in fixing, for instance, the percentage to be deducted from receipts for repairs of fences and cottages. The freedom, however, carries with it an exceptional responsibility, and it is open to question whether it would not be better in this case also to apply the

general rule, and to bring the administration more directly under the control of Parliament by requiring an estimate from the department of the allowances to be made in the course of the year for repairs, etc. A grant in respect of the estimate would then be voted by Parliament in the regular course, and the gross amounts collected would be credited to the Exchequer Account.

We have now seen how the revenue reaches the Exchequer Account of the Treasury at the Bank of England, which is the Consolidated Fund. We have noticed most of the noteworthy deductions which are made from it before it is paid into that account. One other class of deductions, Appropriations in Aid, will be dealt with hereafter. In the cases of the indirect taxes and of one principal direct tax we have followed in detail the actual machinery of collection. With that we have finished with the business of getting, and we pass on to the business of spending.

# CHAPTER V

## SPENDING

We have seen the revenue safely into the Bank of England. There it stays, credited to the Government as a balance on the Exchequer Account, and no man can take it out again save under the authority of Parliament. Parliament provides that authority in the form of a Consolidated Fund Act or an Appropriation Act, as described in the third chapter. Armed with it, the Executive can proceed to draw upon the Exchequer Account to pay its debts.

The process is no simple one. Parliament has hedged it with elaborate formalities. Two chief stages have to be passed through by the state's payments before they come to the hands of its creditors. In the first, they pass from the Exchequer Account to the departments that spend them; and in the second from the departments to the final payees. Let us take them in order.

### Exchequer Issues

By the Exchequer and Audit Act of 1866 the old laws and customs governing issues from the Exchequer were consolidated and modernised, and it is that Act which still rules the matter. The new system which it established, like that which preceded

it, has for its object to secure that no issues shall be made from the Exchequer by the Executive for purposes other than, or for amounts greater than, have been authorised by Parliament.

Parliament, in order to ensure that the money which it votes is properly spent, makes use in the Exchequer and Audit Act of the system of parallel control which we have met several times already. To the Treasury is given power to make issues out of the Consolidated Fund (an *alias*, it will be remembered, for the Exchequer Account), and an independent officer of the House of Commons is appointed to watch it. That is the Comptroller and Auditor General, the high and permanent civil servant who presides over the Exchequer and Audit Department and is independent of the control of the Treasury and of everybody else except Parliament. We are here concerned with him as Comptroller General alone: an account of his functions as Auditor General, which are quite distinct and far more onerous, can be kept till later. Suppose then that the Treasury and the Comptroller General between them are setting to work to get money out of the Consolidated Fund with which to carry on the business of government. No final payments of public money to the state's creditors are made by drafts drawn upon the Exchequer Account at the Bank of England, or in any other way directly out of that Account. Money is issued from the Account in round sums by the Treasury to the credit of the spending departments, and they it is who see to its final disbursement. The issue of a lump sum to a department or other agent of the Government, who spends it and accounts for it, is called an imprest (*prêter*). An imprest is a payment which is not a

final payment but an advance. The procedure of issuing the round sum differs in the case of a sum for a Consolidated Fund service from that in the case of a sum for a Supply service. It will be remembered that a Consolidated Fund service is one paid for out of the Consolidated Fund under authority of a continuing Act of Parliament; a Supply service is one for which money is voted afresh annually in Committee of Supply. Consolidated Fund services include the service of the National Debt, principal and interest, payments to Local Taxation accounts, the King's Civil List, and various pensions and salaries, including the salary of the Comptroller General. Supply services are all the others.

The process of issue on account of a Supply service voted by Parliament is a pompous affair. Grants are made, technically speaking, to the Crown; so the first step in the process of releasing the money granted for use is a Royal Order delivered by the Crown to the Treasury which sets the total grant in a Consolidated Fund Act or Appropriation Act at the disposal of the Treasury.[1] The order recites the grant and desires the Treasury to "authorise the Bank of England to issue from the Exchequer Account, to the accounts of persons charged with the payments, such sums as may be required." Issued under the sign-manual and countersigned by two Lords of the Treasury, it is in fact

[1] Other Orders of the sort are sometimes needed, and made, between the Order in respect of the Consolidated Fund Act, and that in respect of the Appropriation Act. That is the case when the sum taken on account of a particular Vote by the Consolidated Fund Act is exhausted, but the balance of the Vote has since been taken in Committee of Supply and reported to the House. A Royal Order may then be issued setting that balance at the disposal of the Treasury.

issued by the Treasury to itself and is a mere formality, adding no useful check on the process of expenditure. Having provided itself with a Royal Order, the Treasury sends to the independent Comptroller General a formal Requisition, signed by two of their Lordships, "authorising him to grant to the Treasury, on account of Ways and Means for the year ——, credits on the Exchequer Account at the Bank of England for ——." It is the duty of the Comptroller General to see that the Treasury's request for credit is in accordance with the grants of Parliament. Having satisfied himself that it is, he sends to the Bank of England a grant of credit on Supply services for the amount required. Referring to the Treasury's requisition, he writes to the Bank in the following form: "I hereby grant a credit to the Treasury on the Account of the Exchequer at the Bank of England or on the growing balance thereof to the amount of ——, on account of Ways and Means granted for the year ——." This is the critical measure that releases the credit. Having had its power to make the issue verified by the independent control, the Treasury can now get the money. From time to time as the money is required it directs the Bank to issue credits from the Exchequer Account to the Paymaster General on account of the department which is to have the spending of it. When the Bank has done so, it notifies the Comptroller General of the amount and of the destination of the sums so transferred. That enables him to follow the issues of the sums granted, and to see that no issues are made by the Treasury and the Bank for any Vote in excess of the amount granted for it. The Departments also are informed that the sums have been

placed to their credit. Thus each issue out of the Exchequer for Supply services requires the authority of a grant of Parliament, a Royal Order, a requisition from the Treasury to the Comptroller General, a grant of credit by the Comptroller General, and a Treasury order to the Bank of England. The part of the Bank is purely ministerial; but without a grant of credit from the Comptroller General to the Treasury, and a Treasury Order for the issue of credit, it would certainly make no issue from the Exchequer Account. It would have no legal authority to do so, and would run the risk of having to refund the amount to the Exchequer Account out of its own pocket.

The process of issue out of the Exchequer Account for Consolidated Fund services is substantially the same as that for Supply services just described. No Royal Order indeed is needed to put the credit at the disposal of the Treasury; because money for Consolidated Fund services is not granted expressly to the Crown; but, as already observed, that makes no practical difference. At the end of every quarter the Treasury makes out a schedule of the amount required for the Consolidated Fund services then payable in arrear. It requests the Comptroller General for credit to that amount. The Comptroller General verifies the Parliamentary authority and grants the credit to the Treasury. Finally the Treasury orders the Bank to issue the credit to the account of the department which is to make the actual disbursements, and the Bank does so.[1]

[1] The bulk of the war debt charges, unlike the dividends on pre-war stocks, are not payable at the end of each quarter, but at various dates. These, together with any other services which are charged on the "growing produce" of the Consolidated Fund, form the subject of special requests for credit, grants of credit, and orders for issue, from time to time.

Our system for the control of issues out of the Exchequer Account is thus elaborate in its formalities. It is undoubtedly well adapted to serve its purpose, which is to secure that no money shall leave that Account save under the authority of Parliament. That issues out of the Account should thus be checked and guarded is undoubtedly still of some moment. In the Account the money is under the control of the House of Commons. Once out of it, the House has lost control; the money can be spent as the Executive pleases, and, if it is wrongly spent, the House can take retributive and retrospective action only. But now that the responsibility of the Executive to Parliament is established beyond question, the importance of this particular form of control is far less than it was, and our respect for an interesting relic of great historic controversies should not be allowed to mislead us into supposing that the system of checks on Exchequer issues is of the smallest value in enforcing economy and preventing waste. It prevents the spenders from getting possession of more money than Parliament has granted them, or for purposes other than those for which it was granted. But for preventing them from making wasteful use of the money once they have got it, it neither pretends to be, nor is, of any use at all. It prevents money from being used outside the law in a way in which there is nowadays little temptation to use it. It does not prevent money from being wasted within the law, and with the enormous estimates and the ever-growing financial activities of the modern state, it is that sort of preventative that is the urgent need of the hour.

### THE PAYMASTER GENERAL

Before we follow the process of disbursement through its second stage, we must pause for a moment to take notice of a cardinal rule of good financial administration, whether it be that of a private business or of the state. It is the rule that cash balances outstanding in the hands of spending officials should be as small in size and as few in number as possible. Some free cash balances there must be, ready to be drawn upon by the proper officers for the daily needs of the public service. But they should be as small as possible, no greater when they are renewed daily, for instance, than is needed for the service of the day; and they should be as much concentrated as possible. There are several good reasons for that. The first is that money has a value when it is in use; borrowers are willing to pay interest for it. But when it is lying idle as a balance it is valueless, so that a balance is an expensive luxury and the bigger the balance the bigger the expense. That is a good reason for keeping the public balances as small as possible. For keeping them as much concentrated as possible there are good reasons also. The time during which public money is lying free in the form of a balance at the disposal of a spender is the riskiest period of its career. Misappropriations, defalcations, and all sorts of improper uses of it can then most easily be made. Actually in former times, when very large balances were left for long periods in the hands of a number of spending paymasters, it was the regular thing that those who held them should put them out to interest or

speculate with them for their own benefit. Enormous fortunes could be made in that way alone, and the office of a paymaster was the noblest prey of the place-seeker's hunt. The elder Fox followed the bad practice, and founded a fortune; the elder Pitt refused to follow it, and earned a reputation for honesty which was the foundation of his power. Close watch and careful control of free balances are needed, and the fewer separate balances there are, and the smaller, the closer and more careful can the watch and control be made, and the fewer inspectors and auditors are needed to do the work. Finally it is a practical rule that the bigger the balance the smaller the relative margin that need be kept on it above the probable requirements of the day, or of whatever period it is for which it remains unrefreshed. The wider the area, the less the divergence from the average. If money issued daily as an imprest for disbursement be split up for instance into ten balances in the hands of ten spenders, each must keep, it may be, a ten per cent. margin above the needs of the day; but if it be concentrated into one balance, it is found that a five per cent. margin is all that is needed, and so it is a smaller amount that need be left lying about.

In the interests of economy and of the efficient supervision which makes for economy free balances should be as small and as few as possible. For that reason the issues made out of the Exchequer for the public service by the Treasury as imprests to the departments are not split up into different balances, one for each department. They are all kept concentrated in one balance set to the account of a single official whose chief business it is to look after that balance and to spend it for the depart-

ments and under their directions; and that is the Paymaster General.[1] There is statutory authority for this excellent practice: it is Section 11 of the Exchequer and Audit Departments Act, 1866, which says that the sums issued may be considered as constituting part of a general drawing balance applicable to the payment of all services for which the officer to whom they are issued may be accountable. When the Treasury requests the Bank to make an issue from the Exchequer Account, it directs that the sums mentioned shall be transferred, not to the spending department, but to the Paymaster General, "on account of the Supply Service following," and it specifies the service and the amount, following in its specification the classification of Votes in Supply. The Paymaster General banks with the Bank of England, so the issue is made by a mere cross-entry in the books of the Bank, from the Exchequer Account to the Paymaster General's account. But it needs special emphasis that although the purpose for which the issue is made is specified by the order for the issue, there is no earmarking for that purpose of the credit issued. As soon as it is issued it falls into the Paymaster General's general cash balance, which is a single balance and not many balances, and it becomes available for any purpose whatsoever for which he is authorised to make payments.

Between the Paymaster General and a department on whose account he receives issues from the Exchequer the relationship is that of agent and principal and in some aspects that of banker and customer. He pays its debts for it. For this

[1] Who is a figure head, and has his work done for him by an Assistant Paymaster General.

purpose he keeps several banking accounts of his own at the Bank of England. One, the Exchequer Credit Account, more usually called his Supply Account, is a mere record of receipts; to it are paid all issues which he receives from the Exchequer, but no drafts are drawn upon it. Other two, his Drawing Account and his Bill Account, are the accounts from which the actual disbursements are made. There is another important banking account of his, the Cash Account, but for simplicity's sake we will pass it over for the present. Drawing Account and Bill Account are fed daily by writing credits on to them in the books at the Bank off the Supply Account. No more is set free daily from the Supply Account than is needed for the payments of the day. With the day's supply of credit written off from this Account on to his Drawing and Bill Accounts, the Paymaster General is prepared to make the departments' disbursements for them. Out of the Drawing Account cash payments are made, and payments by cheque, by "writes-off" according to a system to be explained, and by sight drafts on the Paymaster General. Out of the Bill Account are met bills of exchange which the Paymaster General has accepted.

When the liability of a department to pay money to somebody is fully matured, it makes out a draft upon the Paymaster General for the amount and gives it to its creditor. Such drafts are signed in the department by a special officer called the Accounting Officer, of whom more hereafter, or his deputy, and countersigned by some other officer of the department designated for the purpose. Daily the departments transmit to the Pay Office a statement of the drafts so made out, which is their

authority to the Paymaster General to make payments for them. Their authorities cover either single payments or series of successive payments. The recipient of the draft takes it to the Pay Office. Payments there are made on the personal application of the payee or of an agent of his, for example his banker, only; the Office will not remit money or cheques by post. At the Pay Office the drafts presented are compared by a large staff of examiners with the authorities received from the departments. If all is well, the payee may get payment in one of several ways. If a small amount only is involved, not more than a hundred pounds. the Office will pay him if he pleases in cash. For that purpose it keeps a small balance of cash on the premises. Every day enough cash is obtained to bring the amount in hand up to a few thousand pounds. The cash is drawn by means of a cheque on the Drawing Account at the Bank. But that covers a tiny portion only of the total payments. For bigger sums, if the payee of the draft has no account with a bank that banks with the Bank of England, he is paid by a crossed cheque drawn on the Drawing Account. To get payment for that he has only to present it at the Bank of England through his own bank. If the payee has an account with a bank that banks with the Bank of England (as all the big banks do), the Pay Office follows another and a preferable course which avoids the risks involved in drawing and presenting a cheque. The payee sends his draft on the Paymaster General to his bank. Next day a clerk from the bank attends at the Pay Office with all the drafts of the sort received that morning from its customers. At the Pay Office the departmental authorities for the payments are verified,

and on the same day an authority is sent thence to the Bank of England to write off the total amount of the drafts from the Drawing Account to the account of the bank in question. Finally the payees' bank splits up the total credit thus received amongst the accounts of its customers. In any case together with his order for payment the payee presents to the Pay Office a receipt, which is retained and sent by the Pay Office to the authorising department as a voucher for the payment, to be used subsequently for purposes of audit. That rounds off the system of checks as between the Pay Office and the departments. As between the Pay Office and the Bank, accounts are checked by a pass-book sent daily from the Bank to the Pav Office, which is compared with the counterfoils of cheques, bills, and authorities for writes-off.

For a class of payments known technically as payments for non-effective services the Pay Office is itself directly responsible. Generally speaking non-effective payments are pensions. It is the duty of the Paymaster General to see that no one gets any money by way of a pension to which he is not entitled, and especially to guard against the personation of defunct pensioners. With other creditors of the state it is the Secretary of State or other head of some department that is their debtor; the Paymaster General stands to them in no such relation. But his relation to a state pensioner is that of a debtor to his creditor. Standing authorities for the payment of the pensions are prepared at the Pay Office itself, and in checking the payments these take the place of the authorities received from the departments in the case of effective payments. Otherwise the business follows the same course.

Such is the method of making direct and final disbursements. To give a full account of the matter one small elaboration is needed as to payments which are not direct and final. There is a large class of payments which has to be made locally and in cash. Soldiers, for instance, have to get their pay in scattered camps and garrisons. To provide for that, money is issued by way of imprest to local paymasters. They receive from their departments drafts for lump sums upon the Paymaster General, and pay them into their local banks. The local banks clear the drafts with the Bank of England through their London Officers or agents, and set the proceeds to the credit of the local paymasters. A balance is thus put at the paymasters' disposal, out of which they make their disbursements, and for which they have to account. In accordance with the principle already discussed these balances are, or at any rate ought to be, kept down to the least sum needed to meet the immediate and current requirements of the local services.

Payments for Consolidated Fund services, as distinguished from Supply Services, also require special mention. All except those for the service of the National Debt are made by the Paymaster General. Quarterly schedules of payments to be made are received at the Pay Office from the Treasury, and on these standing authorities for the payments are prepared. The disbursement, for instance, of money provided for the King's Civil List is made by the Paymaster General in the form of imprests issued to the Paymaster of the Royal Household and to the Keeper of the Privy Purse. Payments on account of interest and principal of the National Debt are not made by the Paymaster General, but

by the Bank of England and the National Debt Commissioners, and we will deal with them later.

### THE VOTE ACCOUNTS

Parliament grants fixed sums for definite purposes; votes in Committee of Supply follow the Votes of the estimates, each of which specifies a particular service and the amount to be spent upon it. Each Vote is a watertight compartment; money granted for one Vote must not be used for another. All Credit issued from the Exchequer is allocated by the Treasury to a particular purpose. In the case of the Navy and Air Votes, leave to make transfers between the Votes can be obtained; but at the end of the year the expenditure on each Vote must not have exceeded the amount granted therefor. To maintain this appropriation of grants in the most rigid manner is one of the chief objects in financial administration. How, it may be asked, is it consistent with the fact that the credit in the hands of the Paymaster General is kept as one general balance, any part of which may be used for any service? To answer the questions we must consider more closely the system of accounts kept at the Pay Office as a record of money spent on each Vote. These accounts of record have no connection at all with the Paymaster General's banking accounts, kept at the Bank of England.

Once more it will be useful to remind ourselves of the difference between an account and a balance. In what we have been saying hitherto of the business of the Paymaster General we have dealt principally with his balance: it is one and indivisible, and all but the few thousand pounds in cash at the Pay Office

and the balances in the hands of local paymasters is kept at the Bank of England. That general balance of his at the Bank is the sum of the four balances standing to his credit on the four banking accounts which are kept for his convenience: his Supply, Drawing, Bill, and Cash Accounts. Now we have to consider a separate and parallel system of accounts, kept at the Pay Office, to show what the balance is being spent on. For simplicity's sake we will consider in the first place the more rigid system of account-keeping applied to Civil Service Votes.

As soon as Parliament has granted Ways and Means to cover Civil Service Votes and a Royal Order has been issued putting the grants at the disposal of the Executive, the Treasury notifies the Paymaster General of the amounts and purposes of the grants. For each Vote for which a grant has been made the Paymaster General then opens a separate account, noting the total amount granted for each. The department which is to have the spending of the money voted is also told. Department and Paymaster General both now know that Parliament has granted certain money for certain purposes. They need not wait for money to be issued from the Exchequer on account of the grants to begin their spending. There is the Paymaster General's general cash balance to go on with: and in the interests of economy that is to be used up before fresh issues are called for from the Exchequer. Forthwith then the department proceeds to draw upon the Paymaster General for the service of the Votes for which grants have been made. The Paymaster General meets the draft out of his general cash balance, and debits the account of the Vote in question with the amount.

Here then are the departments spending public money wholly free from all the elaborate restraints of Treasury Orders and Credits from the Comptroller General on the Exchequer Account. But the liberty to do so reaches a very small way only, for the Paymaster General's cash balance at any given time will not go very far: it would soon be exhausted and payments brought to a standstill were it not refreshed by issues from the Consolidated Fund to his Supply Account. Issues of the sort are made almost daily by the Treasury in order to enable the Paymaster General to keep pace with the payments authorised. Each issue for Civil Service Votes, by the form of the order making it, is appropriated piecemeal amongst the several Votes. The Paymaster General credits to the account of each Vote the amount issued therefor. Sometimes, by the use of the general cash balances, that amount may be overdrawn in respect of a particular Vote. Such an overdrawing leaves a debit against the account of that Vote. The next Credit issued from the Exchequer for the Vote then goes to wiping off that debit. Once a month in the case of Civil Service Votes the Paymaster General balances the Vote Accounts; and if there is a probability of a debit against any one of them at the end of the month, in consequence of his spending on its services more than has been issued for it from the Exchequer, he notifies the Treasury and the Treasury makes an Exchequer issue to meet the probable deficit. At these times the expenditure on account of each Civil Service Vote is completely covered by Exchequer issues, and the Paymaster General's disbursements are fully regularised. It will be observed that one result of this system is that it is only at the end of

the month, when the accounts of the Votes are squared, that Exchequer issues correspond with the actual expenditure on Civil Service Votes. At other times the use of the Paymaster General's General Cash Balances as described prevents any close approximation between the amount of Exchequer Issues and that of the actual expenditure on account of the individual Votes.

The Navy and Air Votes are dealt with at the Pay Office in a somewhat different manner. (It will be remembered that there is now only one Vote for the Army.) In consequence of the practice of allowing grants for one Vote for the Navy to be used temporarily for any other Navy Vote, and so also in the case of Air Votes, issues from the Exchequer on account of Navy and Air Votes are made under those general headings and not on account of particular Votes.[1] In their case, therefore, the unit for accounting purposes is not the Vote, but the sum of the Votes for each. There is no monthly balancing of the two totals, but every quarter a reckoning is made, and issues are made by the Treasury to wipe off any debit and thus regularise the whole of the payments made by the Paymaster General on account of each Vote. Since these Votes (with the Army Vote) are by far the largest, it is only at the quarterly periods that the total Exchequer Issues correspond closely with the total national expenditure. The discrepancy, however, between issues and expenditure is never very big.

Finally at the end of the financial year there is a close and thorough examination of the state of all the Vote Accounts, and every precaution is taken to make the total Exchequer Issues for each

[1] Exchequer and Audit Act, 1866, § 15.

Vote, Naval, Military, Air Force, and Civil Service, correspond with the utmost accuracy with the actual expenditure on each.

Credit issued for the Votes of the expiring year is available to meet orders for payment dated before April 1st; but for economy's sake the Paymaster General may use after March 31st what is left of his old balance issued for the expired year for the services of the new year, as soon as notice is received from the Treasury that Parliament has made grants for the services in question. On the 31st March the accounts are closed, but the balance runs on.

### The Paymaster General's Cash Account

Were the rule that all revenue is credited at once to the Exchequer Account absolute and invariable, we should now have finished the story of the process of spending. But unfortunately it is not. Already we have had to deal with one important exception to the rule, the interception of revenue by the Revenue-collecting Departments, to meet the expenses of its collection. Now we have to deal with another in connection with the business of the Pay Office.

A small part of the revenue is received, not through the great Revenue-collecting Departments, but in the form of casual sums paid to other offices. At the Admiralty and at the War Office, for instance, sums are received in payment for the sale of old stores. With few exceptions, these sums received by departments other than the great Revenue Departments are paid over by them to the Paymaster General. It might be supposed that the departments would have to follow the general rule

and pay the revenue so received by them into the Exchequer Account: but it is not so. An exception is made (in this case as in the case of the interception of revenue by the great Revenue Departments for costs of collection) for the sake of simplicity and economy, on the principle that revenue should be used where it comes to hand. For this reason the Paymaster General is allowed to take these receipts, to credit them, as he receives them, to a special account of his at the Bank of England, which is called his Cash Account, and to use the balance on that account, as part of his general cash balances, to pay the departments' bills with.

Thus to the Cash Account are credited all sums received by the Paymaster General other than those issued to him from the Exchequer Account. It is an account parallel to his Supply Account, and it is used for the same purposes. No payments are made out of it; it is used to refresh his Drawing and Bill Accounts. Here then is revenue which never enters the Exchequer Account at all. It gets as far as the Paymaster General's Cash Account, and then doubles back into his Drawing and Bill Accounts and so out into the pockets of the state's creditors.

There is another source of contribution to the Paymaster General's cash balances. In the course of their business the Government departments receive other large sums, not as final payments, but on deposit. These are not revenue in any sense, and could not be paid into the Exchequer Account without falsifying the total of the nation's income. They are paid over by the departments to the Paymaster General and fall into his general cash balance as part of the balance on the Drawing

Account. A convenient part only of the total amount so received is left as a free balance; the rest is invested. In this category also may be included the balances of two other funds held by the Treasury which for the present are only names to us but which will be explained later, the Treasury Chest Fund and the Civil Contingencies Fund.

Nothing has yet been said as to the way in which the receipts from Departments which are credited to the Cash Account are dealt with in the Vote Accounts. We have seen how the money so received is used, but not how it is accounted for. As has already been mentioned, Parliament in dealing with the estimates in Committee of Supply allocates such minor receipts as Appropriations in Aid of particular votes. As, therefore, they are received and paid into the Cash Account, credit is given for them on the account of the Votes to which they are allocated, just as if they were Exchequer Issues. The more a Vote Account receives in this way, the less it needs to receive from the Exchequer at the periodic balancing.

Very roughly, as we have seen, every month, more fully every quarter, and with great accuracy every year, the Paymaster General's disbursements are brought under the review of the Treasury and subjected to the check of the Comptroller General, and matters are squared up with the Votes of Parliament. But let it be recognised that between whiles the power of drawing upon his general cash balances for payments on a Vote in excess of issues actually made in respect of that Vote from the Exchequer Account imposes upon the Paymaster General part of the high and heavy responsibility of seeing that

the grants of Parliament for any particular Vote are not exceeded. Obviously it would be quite possible for him by the use of his general balance to allow a Department to exceed the total sum granted by Parliament for any Vote. Neither the Treasury nor the Comptroller General could stop him. It is true that he would be brought up sharp by the Treasury as soon as it became necessary to apply for an Exchequer issue to balance the debit against the Vote Account. The Treasury would then answer, "there is nothing more to be issued from the Exchequer for that Vote," and the fat would be in the fire. But to prevent the possibility of so gross an irregularity the Treasury lays upon the Paymaster General a direct personal duty to see that the total sum granted by Parliament for any Vote is not exceeded. He has a note of the total on his Vote Account, and he must see that the payments authorised by a department on account of any Civil Service Vote do not exceed that total, and that those authorised for Naval and Air Services do not exceed the totals of their respective grants. "The Paymaster General," says the Treasury,[1] "will not make a payment under any head of service exceeding the balance remaining on the grant of Parliament for that service; and will keep in his books separate accounts of the grants remaining in the Exchequer and in his hands, under the several heads of the service, that he may be prepared to exercise an efficient check upon the accounts of the application of the Votes of Parliament, and to submit to this Board any order for payment which may be drawn upon him in excess of the available balance of the grant unissued from the Exchequer, or in

[1] Treasury Minute. 22/12/1848.

his hands, to which such order may relate." Thus for the all-important purpose of preventing departments from spending more upon a Vote than Parliament has granted for it the control of the Paymaster General, who does the spending, is the first line of defence, and that of the Treasury and of the Comptroller General are the second only.

The system of a generalised balance and that exception to a good rule which allows minor receipts to escape the control of a passage through the Exchequer Account allows plenty of opportunity for irregularities. To prevent them the chief check is the rule that the Paymaster General, although he may make disbursements in advance of Exchequer Issues, must make no payment for any service until he is notified that Parliament has granted money for it, and that the money has been placed at the disposal of the Executive. It is, therefore, of importance to grasp at what point in the process of parliamentary authorisation of expenditure the Treasury is at liberty to notify to the Paymaster General that money is available for the service of a Vote. The critical point is the issue of the Royal Order which sets funds voted at the disposal of the Treasury. As already stated, the Royal Order can be issued as soon as a Vote has been passed in Committee of Supply and Reported, without waiting for the resolution in Committee of Ways and Means or for the final statute, Consolidated Fund Act or Appropriation Act, that gives the proceedings of the Supply Committee the full force of law. But that is on one condition. The Order can only be issued on the strength of the resolution in Supply if there are grants enough to cover the expenditure still unexpended, which have been authorised for the

service of the year by some previous Consolidated Fund Act. Funds voted in Ways and Means and legalised by a Consolidated Fund Act, it will be remembered, are voted generally; they are not appropriated to any particular Vote. The Consolidated Fund Act authorises the Treasury to issue a certain sum and apply it towards making good the supply granted for the service of such and such a year. According to this wording, it matters not whether the supply be granted before or after the Act is passed. A Royal Order may, for instance, be made to set at the disposal of the Treasury Ways and Means voted in respect of the Votes on Account and legalised by the Consolidated Fund Act, for use in respect of grants voted by the Committee of Supply after the Consolidated Fund Act became law, and that is often done.

# CHAPTER VI

## APPROPRIATION AND AUDIT

HITHERTO we have been concerned with the practical work of getting and spending. We have seen Departments estimating how much they will need to spend in the coming year; Parliament authorising expenditure according to the estimates, and saying how the money is to be got to meet it; the revenue departments getting the money; and the spending departments, through the Paymaster General, spending it. Now we turn from the practical business of legislation, of the collection and expenditure of revenue, and the manner in which they are organised and controlled, to paper processes of accounting.

In private life a very careful man keeps accounts from day to day to show him how much he is getting and how much he is spending, so that he may be sure at all times that he is not running into debt. A State has to be even more careful than that: it has to plan its expenditure and income beforehand, and to draw up anticipatory accounts of them as a guide to itself and to its servants in their subsequent proceedings. At the beginning of the year the State draws up accounts of how much it is going to spend, those are the estimates; and it makes another account of how much it is going to

get, that is the budget scheme. Having made the two balance by reducing estimated expenditure or increasing estimated revenue, it has done with its principal account-keeping for the year. In theory everything is now to take place exactly as the estimates provide. Spenders are sent off to spend and collectors to collect according to the estimates and the authority given them, and at the end of the year the anticipatory and estimated accounts would, in a perfect world, stand as realised accounts. But Parliament is not content to rest in the simple faith that every spender will do exactly what he is told, neither spending a penny more than he is authorised to spend, nor spending on one service the money voted by Parliament for another. In the days of its struggles with the Crown it learnt the vanity of content with a formal grant of credit, without supervision of the way in which the credit was spent. In its struggle against the Executive for the control of finance its first victory was to make the Executive come to Parliament for money, and to prevent it from getting money elsewhere. Its second victory was to gain the right to say upon what the money which it voted was to be spent. But that was not enough. It was all very well to appropriate the money voted for a specific purpose, but what was to prevent the Executive, once it had got the money out of Parliament, from snapping its fingers at Parliament's directions as to appropriation, and from spending it as it pleased? It was not until at least a century after the time at which Parliament established its right to appropriate that it woke up to the inadequacy of a formal appropriation, to secure its purpose, unless it exercised some supervision over the actual expenditure.

During the first half of the nineteenth century it was becoming clear to financial reformers that the active enforcement of the appropriation of grants, even after they had been released from the control of Parliament for the use of the spenders, was a necessary coping-stone of the structure of Parliamentary control over finance. The financial genius of Gladstone gave the principle clear expression. "It is undoubtedly the business of the House of Commons," he said, "to be responsible, not only for the inception of all public expenditure, but also to follow money raised by taxation until the last farthing is accounted for." [1]

The lesson had by then been learnt that to support the power of Parliament in money matters it is necessary that Parliament should not only direct how the money is to be spent beforehand, but should see that its directions are carried out. It cannot of course watch the spending of money from day to day throughout the year. But what it can do is to require at the end of the year an account of how the money has been spent, and evidence that it has been spent on the purposes to which it was allocated by the votes in Supply and appropriated in the Appropriation Act. Knowing that there is such a reckoning before him an official spender dares neither to spend more than he is authorised to spend, nor to divert money from the purposes to which Parliament appropriated it. Were he to do so, he would be detected at the *ex post facto* revision of his expenditure, and a surcharge would be the penalty for his illegal act.

[1] Hansard, Vol. 197, p. 633.

## Appropriation Accounts [1]

Monopoly in the granting of public money, the right to direct how the money which it grants is to be spent, and the power to see that the money which it granted has been spent as it directed, these are the three essential constituents of a full control by Parliament of revenue and expenditure. The third essential was secured by the Exchequer and Audit Act of 1866. By that Act it is provided that every spending department is to render to Parliament, at the end of the financial year, an account of the way in which it has spent the money voted for it by Parliament. Those accounts, which show how the money voted has been appropriated, are called Appropriation Accounts. They are the coping-stones of the financial structure of the year. By their means the expenditure of the year is brought under the review of Parliament, and Parliament is enabled to watch and see that no money has been spent for any other purpose than that to which Parliament appropriated it.

In a world in which nothing ever happened contrary to expectation, the Appropriation Accounts would be a replica, word for word and figure for figure, of the anticipatory accounts as set out first in the Estimates and finally in the schedule to the Appropriation Act. Their purpose is to enforce the legal duty of adherence to that schedule, and were there no deviation from the legal duty, authorised or unauthorised, they would show that the money had been spent penny for penny as the schedule provided. In this bad world in which it is the

[1] Examples of Appropriation Accounts will be found in Appendices A. and C.

unexpected only that comes to pass, it is necessary to make some provision for the authorisation of deviations from the schedule in case of emergency, and at the end of the year it may turn out that, intentionally or unintentionally, some deviations have been made from it that were unauthorised. Authorised deviations we will consider hereafter; for the present in dealing with the preparation and examination of the appropriation accounts we may leave them out of account, and deal with the accounts as if they were records of expenditure by the departments which has accorded exactly in every detail with the scheme of appropriation in the schedule, and in so far as they show deviations therefrom are irregular and censurable. In form these accounts follow accurately the form of the estimates and the schedule, Vote by Vote and subhead by subhead. They show the original and the supplementary grants of Parliament for the year, as a charge, and against them and in discharge of them the sums which have actually come in course of payment in that year. They show also the estimated amount of receipts to be appropriated in aid of grants, and the sums actually realised in respect of the same.

Obviously it is for the party who does the spending to account for what he has spent. Each department which presents an estimate and receives a grant must prepare also an Appropriation Account, to show how the money granted has been spent. But Parliament is not content with any general or collective responsibility in a whole department for an Appropriation Account. For greater security it now requires that in each department that renders an Appropriation Account there shall be a single official, called the Accounting Officer, who shall

have a direct and personal responsibility for the Account.[1] When the Account has been drawn up in the department, the Accounting Officer signs it with a declaration that to the best of his knowledge and belief no part of the expenditure contained in the Account has been incurred without authority superior to that of the department, in cases where such superior authority is required. The account is sent to the Treasury, and to the Comptroller and Auditor General, who examines it on behalf of the House of Commons. It is then laid before Parliament. Containing as it does a detailed statement of all sums which came in course of payment during the financial year, the Account cannot be completed until some time after the year has come to an end on March 31st. In general it is not until the following January that the Accounts are presented to Parliament, in time to be considered in the new session.

### The Public Accounts Committee

Many documents submitted to Parliament, when they have been laid before it and have been ordered to be printed, have received all the attention from Parliament that they ever will receive. But the House of Commons is not content with a merely formal reception of the Appropriation Accounts.

[1] Under the Exchequer and Audit Act, 1866. Section 22 of that Act provides that the Appropriation Account is to be prepared by the *Department* charged with the expenditure of the Vote, and adds that the term "Department" is to be construed to include any public officer to whom the duty may be assigned by the Treasury. The Treasury has in fact assigned the duty to a special officer in each department; and the Public Accounts Committee and Parliament have often approved and enforced that arrangement.

It is not content to take it for granted that its directions as to the appropriation of public funds have been carried out; it imposes upon itself the tasks of careful and minute scrutiny of the accounts, of inquiry into all irregularities, and of admonition and, in case of final need, of punishment of peccant officials. For the performance of these duties close consultation with the Treasury is necessary and the examination of witnesses and of documents. The House itself would be quite unable to do the work; it would have neither the time nor the means; so it entrusts the task to a Select Committee, called the Public Accounts Committee, which is appointed for "the examination of the accounts showing the appropriation of the sums granted by Parliament to meet public expenditure." First established by Gladstone when Chancellor of the Exchequer in 1861, the Committee has ever since been annually reappointed towards the beginning of the session in January or February. It numbers fifteen members; according to custom its chairman is generally a member of the Opposition and amongst its members is the Financial Secretary of the Treasury. Members of every party are elected to it, and especially any member who may be distinguished by a knowledge of public finance. At most times the Committee, and through the Committee the public, have had the advantage of the services of one or two members who have made finance their study, and have laboured there for the maintenance of the highest standards of financial rectitude, at a sacrifice to themselves of time, energy, and personal political interests which has been to the very great advantage of the nation. Many gallant stands have been made at that Board for

order, regularity, and economy in the methods of public finance.

As soon as appointed by the House, the Committee takes the Treasury in one hand and the Auditor General in the other, and goes a-hunting in the expenditure for the year under review, as certified in the Appropriation Accounts. The Auditor General beats the bush and starts the hare: the Committee runs it down: and the Treasury breaks it up. Reports are prepared for the Committee by the Auditor General on the Appropriation Accounts and all other matters into which he has inquired in his preliminary investigations. He, it will be remembered, is the servant of the House of Commons and of its Committee, responsible only to them and to no other master. Nine-tenths of the Committee's inquiries are concerned with points which he raises. Any member of the Committee may raise any relevant question on his own initiative, but in practice the Committee works on the Auditor General's brief. He sits with them at the Board, and gives them help. A high Treasury official also is always present to advise them. In their decisions the Committee and the Treasury are generally in hearty agreement. Their point of view in these matters is the same: both are concerned to enforce regularity and economy in the administration of the departments, and the Committee is the rod which the Treasury has been shaking over the heads of the Civil Service throughout the year. When the Committee's decision has been recorded, it is for the Treasury to take the matter up with the department concerned. If the Committee has censured something, the Treasury communicates the censure,

adds its own, and tells the department that it must not happen again. It is common indeed to find an opinion expressed with judicial mildness by the Committee enforced with far stronger language by the Treasury in communicating it to the department. Where the Committee has roared as mildly as a sucking dove, the Treasury roars like a Libyan lion. Very seldom the Treasury does not agree with the Committee. Special attention is then called to the disagreement in the report to the House of Commons with which the Committee ends its labours, and it is for the House to take action if it pleases, which it very seldom finds time to do.

This is the last stage in the history of national finance for a year. The Report of the Public Accounts Committee is its epitaph. It may not be until late in the session that the Report is received. By then the departments are already beginning to think of their estimates for the next year. Nearly three full financial years are thus needed to complete the life-history of a year's finance. A beginning is made with the estimates for the financial year 1924–1925, for instance, in October, 1923. Appropriation Accounts for 1924–1925 are presented in January, 1926, and it is not till late in that year, it may be not until an autumn session, that Parliament finally disposes of them by receiving the Report of the Public Accounts Committee. Having done so, it has completed its task under the system of control which it has devised to maintain its power. It has granted the money needed, it has appropriated the sums granted to specific purposes, and through the Public Accounts Committee it has seen that its orders as to appropriation have been obeyed. As regard the finances for the year reviewed Parliament

is then *functus officio;* and it leaves their dead record for a prey to the statistician.

### Accounting Officers

From what has just been said it will be clear that the great value of the control of expenditure exercised by the Public Accounts Committee is due in large measure to the preliminary investigation made on behalf of the Committee, and in discharge of his statutory duties under the Exchequer and Audit Act, by the Auditor General. As his name shows, the investigation which he carries out is in the nature of an audit. In making it he must make use, in the first place, of the Appropriation Accounts supplied to him by the Accounting Officers of the departments. These Accounting Officers are an essential element in the processes of audit and control. As already mentioned, their chief duty is to render the Appropriation Accounts to the Auditor General, showing how the grants of Parliament have been spent. They sign the accounts and are primarily responsible for their correctness. But their responsibilities are far higher than those of a mere accountant, and the consent of the Prime Minister is required for their appointment (or removal). Each in his own department is the guardian of the scheme of appropriation authorised by Parliament. Each is responsible to the head of his department and to the Treasury that no money is spent by the department otherwise than as authorised by Parliament. To discharge that responsibility, they must either themselves or through their subordinates of the financial staff of the office follow the payments made by the departments day by day, and assure

themselves that each is duly supported by Parliamentary authority. They cannot of course investigate every payment, and see that it is actually made as it professes to be made: but they must take reasonable precautions. It is incumbent on them before making or allowing payments to satisfy themselves by means of certified statements from the officers entrusted with the detailed duties of payment that each payment is legal. They are entitled to consider that a statement of the sort is enough for them. If they can show that they have not acted except on such statements, with common sense, and after consulting a Treasury expert in case of doubt, the Committee and Treasury consider that they have discharged their responsibility as regards payments which are on the face of them legal.

To discharge his responsibility for a payment which is on the face of it illegal is for an Accounting Officer a harder matter. It is to be observed that he is an officer of his department, and not even in his function as Accounting Officer a servant of the House of Commons or of the Treasury. He cannot therefore simply veto such a payment. Had he the power to do so, that would involve two ill consequences: it would destroy the salutary responsibility of the Head of the department for the expenditure of his department, and it would lead to friction and even to deadlocks in the working of the machinery of administration. But the unfortunate Accounting Officer must not be fixed with an inevitable responsibility for irregularities or illegalities which he is unable to prevent. A way must be given him to shift the responsibility on to other shoulders, once he has done his duty

*by doing his best to stop the illegal payment.* His means of escape are by shifting the responsibility on to the shoulders of the supreme chief of his department. He alone has power in the department to override the Accounting Officer's decision that a payment is irregular or illegal. If such a payment is proposed and the Accounting Officer's protest is disregarded by subordinates, he must carry the matter to the Head of the department. He must make known to him that the proposed payment is irregular, and that there are no funds legally available to meet it. If the Head does not support him, he must obtain from him a written authority to make the questioned payment. Having obtained that he has done his best, and is immune when the rendering of the Appropriation Account discloses the irregularity to the Treasury. Without it he is personally liable to make good the irregular payment, and his liability, if the Public Accounts Committee disallows the payment in question, can then be removed by a Vote of Parliament only.

Mention has been made before this of the anxieties attaching to the free balances of public funds once they have come into the hands of the spenders. The funds in the hands of a department consist of (*a*) a balance with the Paymaster General, (*b*) balances in the hands of its own Officers, called in this capacity sub-accountants, which have been issued to them as imprests from the Paymaster General's balance. It is the latter that are referred to here as free balances. Pains are taken to keep these free balances as small as possible, but some of the departments have to meet local payments and so on from day to day, and somebody must be responsible for them. This respon-

sibility is imposed upon the sub-accountants by whom the imprests are received. It is shared by the Accounting Officer. He must remain responsible for all payments made by sub-accountants out of imprests, because just as much as the final payments made by the Paymaster General for his department they are charges against the Votes for which he is responsible. He must, therefore, take all reasonable precautions to ensure against misuse of the balances. He must see that no sub-accountant holds unnecessarily high balances, or delays to render his accounts; and he must see that money is entrusted to those officers only who are of a standing commensurate with the balances which they keep, and so on. But the personal responsibility of the sub-accountant who has the custody of the balance is the foundation of the system by which the use of the free balance is checked and controlled. Thus the Accounting Officer answers for the money which has passed out of the custody of the department, and he and his sub-accountants answer for the balance which still remains in its custody; and so an account is given of every penny that the department has received.

In the relations between the Accounting Officer and the sub-accountants there are certain difficulties, difficulties which arise out of the distribution of authority and responsibility between the financial and the executive staffs of an office. To explain their nature, let us consider an example of the practical working of these arrangements. At the Admiralty, for instance, the Accounting Officer is the Secretary. There are sub-accountants in the Paymasters on board each ship. The Accountant General, acting in this case as the deputy of the

Accounting Officer, corresponds directly with them, and they make representations directly to him. But a ship is *imperium in imperio*, and the authority of its ruler, the captain, must be kept absolute. Out of deference to this rule of the Navy, the Sub-accounting Officer on board must make any payments which the captain authorises, and if they are irregular must make his representations on the subject to his financial chief through the captain. On the other hand, the captain cannot block a representation of the sort or refuse to forward it. In such relationships it is obvious that there are openings for jealousy and friction between the executive officers who have got to get the work done and the financial officers on whom is imposed, by Parliament and the Treasury, the duty of acting as guardians of the Parliamentary scheme of appropriation. History, in fact, tells of more than one effort on the part of the more powerful spending departments to get rid of the independent authority of the Accounting Officer and his sub-accountants (an authority, it is to be remembered, which being subject to the supreme chief of the office is only partially independent) by subjecting it to that of subordinate executive officers, or by transferring the functions bodily away from the financial staff to executive officers. In 1905, for instance, an Army Order was published which transferred the powers of certain sub-accountants to a class of military administrative officers. By making the spenders themselves judges of the legality and regularity of their own spending, the Order struck at the root of the whole system of control as established by Parliament. No harm was done, because the attempt was frustrated by the energetic action of the Public Accounts Committee.

It served indeed a useful purpose in moving the Committee formally to emphasise the supreme importance of the position of the Accounting Officers in the maintenance of Parliamentary control over expenditure, and to make a clear statement of the powers and duties secured to them by Parliament in order that they may do the work which Parliament requires of them, and which the Executive must not seek to qualify. The Committee affirmed "the necessity for maintaining unimpaired the established system of accounting to Parliament for appropriation of public moneys to the purposes for which they are intended by Parliament to provide," and declared "that neither can the existing system of Parliamentary control nor the strict responsibility attached by it to the Accounting Officers appointed to carry it out, be removed, otherwise than by Parliament itself." To remove doubts, the Committee recommended that it be laid down that "(1) in the case of the Army, as of all other departments, the duty of accounting for moneys received, expended, or in hand, and the responsibility for them lies upon the Accounting Officer of the department; (2) the authority over, and responsibility for all Sub-accounting Officers [more properly called sub-accountants] belongs to him; (3) no part of that authority or responsibility can be diverted to any other person whatever; (4) in all matters of account, and of payment or receipt, in dispute or not, the Sub-accounting Officer is authorised and required to communicate directly with the Accounting Officer." [1]

The duties and responsibilities of an Accounting

[1] Public Accounts Committee First Report, 1905.

Officer evidently could not be imposed with propriety upon a subordinate officer of the department. "The officer entrusted with these duties," the Treasury has declared, "should occupy a sufficient standing to enable him not only to exercise a direct supervision and control over the persons executing the detailed business of account and book-keeping, but also to influence the working of the department in all those respects which affect the method of its receipts and expenditure. He must also be qualified to represent his department before the Committee of Public Accounts." The conclusion is that the duties of Accounting Officer should be discharged by the Permanent Head of the department, and that is the general rule.

## THE APPROPRIATION AUDIT

As between the Accounting Officers and the Auditor General there is no relation of official chief and subordinate. Appropriation accounts are rendered by the Accounting Officers to the Auditor General, and they are bound to supply him with information on all matters into which he is authorised to inquire. But they are not even for any limited purpose his servants; they are the servants of the departments in which they work. The functions of the Auditor General are in no way administrative or executive even in matters of account; his business is only to watch, search, inquire, and report. It is the verification on behalf of Parliament of the Appropriation Accounts which he receives from the Accounting Officers that is his chief end as an official. For this purpose he examines them, calls attention to irregularities, such as grants exceeded or other

receipts improperly applied, and finally certifies them to be correct. But a mere superficial examination of the accounts themselves is not enough for his purpose. For the better detection of the irregularities and illegalities, he has to conduct a regular audit, acting in much the same manner as a commercial auditor would act.

The essence of an audit of accounts is that it is an investigation into them, made in detail by an independent person not concerned in drawing them up, to ascertain whether they tell the truth, the whole truth, and nothing but the truth about the transactions which they profess to record. For this purpose the auditor must ascertain in the first place whether the accounts presented to him accurately record and summarise the transactions of the period which they cover, as entered from day to day in books of account and other documents, and in the second place whether all payments and receipts for which credit is given and taken in the accounts have actually been made and received. For the latter purpose he must examine and verify the vouchers for payments and other documentary evidence of incomings and outgoings, seeking in particular to detect cases in which there is no proof of payment of sums charged, or in which a payment has been charged out of time. Such is the character of the audit conducted by the Auditor General on behalf of Parliament. It differs from a commercial audit in one important characteristic. It has a different object. A commercial audit has for its final end to see whether, in the balance-sheet that states the position of a business at a given moment, assets and liabilities are properly and accurately evaluated. It is a valuation audit.

The final end of the audit conducted by the Auditor General is to see whether the money granted by Parliament has been spent on the services to which Parliament appropriated it. It is an appropriation audit. Each arrives at its end in the same way, by verifying the statements made in the accounts, to see whether they are truly made. But when they have been verified, the commercial auditor has to ask himself the question, "Have I found out anything which shows that assets are put too high in the balance-sheet, or liabilities too low?" whereas the question which the Auditor General has to ask himself is, "Have I found out anything which shows that money has been spent in a manner not authorised by Parliament?"

It is the Exchequer and Audit Acts of 1866 and 1921 that impose these duties upon the Auditor General, directing him to examine every Appropriation Account and to satisfy himself that the money expended has been applied to the purpose for which the grant was intended to provide. In order to clear our minds of the possibility of confusion, we may here recall that under that Act the Auditor General of the Public Accounts is also the Comptroller General of Receipts and Issues of His Majesty's Exchequer. With his functions as Comptroller General we have already dealt: they are the ministerial control of issues from the Exchequer as imprests to the departments, in order to secure that no issue shall be made therefrom except under the authority of Parliament. We are now concerned with his function as examiner into the expenditure of the imprests after their issue, in order to see whether any part of them has been spent in a manner which Parliament has not authorised, a function

which is less ministerial than judicial. Its judicial character is recognised in the incidents of his office. The Auditor General, like one of His Majesty's judges, holds office during good behaviour: he is removable only by an address to the Crown from both Houses of Parliament. He is appointed by Letters Patent. His salary and pension, like a judge's, are secured on the Consolidated Fund: they are not subject to an annual vote of Parliament. Like a judge he may hold no other office, and may not be a member of either House of Parliament.

His functions as Comptroller General take up little of his time, or of that of his office, which is the Exchequer and Audit Department; they are a formal affair. It is his work as Auditor General that keeps him and his staff busy. To help him he has a secretary and a hierarchy of directors, deputy-directors, and auditors. They do not all sit and work in his office on the Victoria Embankment. For the greater convenience of its work, part of the staff occupies quarters at the War Office, the Admiralty, and the Air Ministry, and a permanent staff is also maintained at the big centres of local naval and military expenditure at Chatham, Devonport, Portsmouth, and Woolwich. In addition a part of the staff is now attached to some of the larger civil departments.

To the officials of this department come daily, monthly, and yearly the accounts of the spenders and the vouchers for the payments which they have made. There is no annual spasm of activity; the processes of audit are continuous. Vouchers for payments in the form of receipts and so on are returned from the Pay Office, as we have seen, to the departments on whose behalf the payments

were made. Other vouchers come in from the local paymasters of the departments. They all are sent to the officers of the Exchequer and Audit Department, either those on the premises or those at the offices of the department on the Embankment, together with counterfoils, bankers' pass-books, and any other books and documents which are essential to the system of checks and relevant as evidence of payments. A large staff of auditors scrutinise the vouchers, bring questionable matters to light, and enter them in journals. A deputy-director decides the less important cases; a director or the secretary decides those of more importance; and matters of general principle are reserved for the attention and decision of the Auditor General himself. Queries are sent to the departments concerned about all matters thus unearthed which are considered to need explanation, and the department returns its answer. If the Auditor General is dissatisfied with the answer, and further inquiry fails to clear the matter up, it is entered on his report and goes before the Public Accounts Committee. In these inquiries the Auditor General's chief channel of communication is through the Accounting Officers in the departments. He is entitled to look to them for the information which he requires, and other officers of the departments are bound, through them, to give him that information.

It might be supposed that the final stage of the audit would be to check and test the cash balances in the hands of the sub-accountants of the departments at the close of the financial year. That certainly seems a necessary step in order to complete the verification of the accounts. But the Treasury has laid it down and the Public Accounts Committee

has agreed that that is an administrative duty, and not part of the functions of the Auditor General. Primarily, no doubt, the responsibility must be that of the department which holds the balance, and as already mentioned of its sub-accountants and of its Accounting Officer in particular. But an external check upon the department would be a very valuable additional safeguard, and need not qualify its responsibility.

The Treasury has the right to verify balances, through the Treasury Officers of Accounts, its specialists in all accounting matters. In practice, however, they do not verify balances unless there is some ground for a special inquiry, but confine their attention to seeing that the machinery for verification by the departments themselves is working regularly and well. The Auditor General, moreover, does in practice call attention to anything which seems to him questionable in the state of the department's cash balances.

In the case of civil spending departments the audit carried out by the Auditor General covers a large proportion, and often the whole of the accounts of each department. It used to be the rule that the whole of these accounts must be examined in detail, but the increase of work has been so large that the staff employed and the cost of audit would be very largely increased by the continuance of a full examination. Accordingly, the Act of 1921 gives the Auditor General discretion "after satisfying himself that the vouchers have been examined and certified as correct by the accounting department, and having regard to the character of the departmental examination," to dispense with further evidence of payment in any particular case.

As regards Army and Navy accounts, the difficulty of auditing in bulk has always been recognised; and these accounts, like those of the Revenue Departments, have of course already been more fully examined than the others, since each of these departments has a special financial branch. The Act of 1866 therefore did not require the Auditor General to carry out a 100 per cent. examination, but left him a discretion similar to that now given generally by the 1921 Act. The audit of Army and Navy accounts has therefore always been a test audit. Instead of auditing the whole accounts of those departments every year, the Auditor General takes a portion of them as a sample of the rest, and tests that. About a sixth of the whole Naval and Military accounts is thus tested every year, so that the whole is audited about once every six years. Pains are taken to dodge about in order that the department may not know for certain what parts of its accounts will have to face the scrutiny at any given time. Of the staff of the Auditor General at the War Office, for instance, two-thirds of those engaged on the Test Audit make an examination of the schedules of the Heads in rotation, but one-third carries on a roving test over the whole range of the Vote.

In the case of the great revenue collectors also, the Board of Customs and Excise, the Board of Inland Revenue, and the Post Office, which all have their special financial branches, the appropriation audit is a test audit only. But having thus tested their accounts of expenditure, the Auditor General has not finished with them. He has also to audit their accounts of receipts. This also he does by a test audit. His officers visit

every year some of the principal local centres of receipt, at the offices of the Board of Inland Revenue in certain large towns and at the offices of the Board of Customs and Excise at big distilleries and so on, and make a test examination of the local accounts, to see that the revenue received has been duly brought to account. Nor are the minor receipts of other departments neglected. They are audited in the course of the general and inclusive audit which is applied to their Appropriation Accounts, in which the bulk of them are entered as Appropriations in Aid.

It is generally recognised that the business of auditing revenue receipts is one of special difficulty. An accounting officer must always be eager to account for all the expenditure of his department; but he may be more inclined to stretch a point in accounting for receipts. No obliquity is suggested: there are many ways of making receipts appear less than they might be made to appear, and an obvious reason for doing so, without anything remotely approaching dishonesty, is the desire to give a favourable complexion to the accounts of a department. It is fairly sure that all payments will be brought to the notice of the auditors on the face of the accounts and subjected to their examination; but they have no means of knowing whether the records exhibit all the receipts, or whether, which is another aspect of the same matter, all proper claims have been enforced. In testing the revenue side of accounts the auditors must look and see whether the administrative regulations and procedure effectively check the assessment and collection of revenue, and they must satisfy themselves by their examination that the regulations are

enforced by the department. Having done that, they have done all that auditors can.

To finish the story of the Appropriation Audit, it may be said that the accounts of the Exchequer and Audit Department are themselves audited; and since no man should be judge in his own cause, they are audited not by the Auditor General but by a Treasury official, to whom the accounts of the department are rendered monthly. It is the same Treasury official who fulfils another special function as auditor, that of the Auditor of the King's Civil List. To secure the privacy and maintain the dignity of the King's affairs, that audit is committed to this single individual and not to the comparative publicity of the Audit Department.

### Stores and Stock-Taking

Stores and Store Accounts, stock and stock-taking, are matters that lie heavy upon the minds of those responsible for economy and for the prevention of waste and leakage in the expenditure of public money. To abandon the watch over expenditure as soon as money has been converted into stores would be to close the eyes and turn them away just when control becomes most difficult and most necessary. Balances at banks and payments out of them are far easier to guard than articles lying about in store-houses, and it is far easier to tell whether a cash payment has been properly made than whether a bunkerful of coal, for instance, which yet represents cash, has been properly distributed. It is therefore eminently necessary that the expenditure of stores should be subjected to a control at least as stringent as that to which the

expenditure of money is subjected. To this necessity Parliament is now awake, although it did not awaken to it until long after the institution of the audit of money payments. That was finally regularised, as we have seen, by the Exchequer and Audit Act in 1866. It was not until over twenty years later that the Admiralty and the War Office, the two great consumers of stores, were directed by Act of Parliament[1] to prepare annual accounts of the value of the stores expended in the Government dockyards, ordnance factories, and manufacturing establishments. The accounts are to include also particulars of the distribution and cost of labour employed. It is directed by the Exchequer and Audit Departments Act, 1921, that stock or store accounts shall be kept in all cases where, in the opinion of the Treasury, the receipt, expenditure, sale, transfer or delivery of any securities, stamps, provisions, or stores the property of His Majesty in any Government department is of sufficient amount or character to require the keeping of such accounts, and the Comptroller and Auditor General shall, on behalf of the House of Commons, examine any such accounts so required to be kept in order to ascertain that adequate regulations have been made for control and stock-taking and that the regulations are duly enforced and that any requirements of the Treasury have been complied with. These accounts for stores are analogous to the Appropriation Accounts for cash. Like the Appropriation Accounts, they are based on a forecast included in the Estimates. In the Navy estimates, for instance, appears a statement of Estimated Receipts and issues of

[1] 52 & 53 Vict. c. 31, § 1. (Extended to the Air Force by Order in Council in 1918.)

Naval stores, etc., during the coming year, showing the value of stock in hand at the beginning and end of the year. When the year is over and the store accounts are made out, they show how far the estimate has been realised, and what departures have been made from it.

Verification of stores in hand, which is called stock-taking, is a process analogous to that of the verification of cash balances in hand, and it is accordingly managed in the same way. The Treasury has decided, and the Public Accounts Committee not without doubts has assented to the decision, that the one like the other is an administrative process, and that it is the business of the department concerned, and not of the Exchequer and Audit Department. But it is recognised that it is a process in which exceptional vigilance is necessary. Public stores, as the Treasury has eloquently said, are lying scattered about over "yards, wharves and shops, in railway trucks or barges, in barracks, forts or camps, by the ship's side or at sea."[1] So, while reserving the business of stock-taking to the departments themselves it has been careful to lay down the conditions for efficiency under which it must be done. As in all other matters of financial control, the chief condition for efficiency is that the check for economy should be parallel to the executive work, that the stock-taking should be done by special officials of the department wholly unconnected with its store-keeping branch. Statements are made and certified, by the special officials appointed for the purpose, of the stock in hand, and in general these state-

[1] T.M. 19/8/1894; to 4th report of Public Accounts Committee, 1894.

ments are accepted as conclusive by the Auditor General for the purpose of comparison with the balances of stock which the stock ledgers show as remaining on hand. For additional safety in the matter one further power is conferred upon the Auditor General; if he sees reason to be dissatisfied with the department's own stock-taking in respect of any particular articles, he may call upon it to take stock of them in the presence of himself or his officers. With his hands thus strengthened his control of stock in hand is greater than his control of cash balances, into which he has no recognised power to inquire, and the interests of economy are thus at least as well served in the matter of expenditure of stores as in the matter of expenditure of cash. In both cases outgoings and incomings are subjected to the Auditor General's test audit. In both cases, balances in hand are subjected to a semi-independent verification, in the case of cash at the hands of the Treasury Officers of Account, and in the case of stores at the hands of independent officials of the department. And in the latter case, in which the ordinary verification is of a less independent nature than in the former, the control is strengthened by the Auditor General's power to call for a special examination in his own presence of any questioned article.

### Trading Accounts

A further class of accounts is dealt with by the Exchequer and Audit Departments Act, 1921, which enacts (Section 5) that "there shall be prepared in each financial year in such form and by such Government departments as the Treasury may from time to time direct or approve, statements of account

showing the income and expenditure of any shipbuilding, manufacturing, trading, or commercial services conducted by the department, together with such balance sheets and statements of profit and loss and particulars of costs as the Treasury may require." All such accounts must be examined by the Comptroller and Auditor General who "in his examination shall have regard to any programme of works, shipbuilding or manufacture, which may have been laid before Parliament."

### Grants in Aid

There is one sort of expenditure which escapes the control of the scheme of appropriation and of the appropriation audit. When the Government wants to help some scheme or object which needs money, but does not want to treat it as if it were a scheme or object of its own, its plan is to vote a grant of money for it which is handed over as a free gift. Grants of the sort are called grants in aid. There are three chief classes of them: (*a*) grants to bodies not controlled by the Government, such as a grant of £1250 a year to the Royal Geographical Society; (*b*) purchase grants for the State's museums and galleries, such as the National Gallery; (*c*) grants to help poor colonies, like Uganda, to make both ends meet.

Of such grants the distinctive feature is that each is paid over in a lump to its recipient, and that no detailed account is required of the manner in which it has been appropriated. He who pays it over is the Accounting Officer, and he discharges his obligation in the matter of account by producing a receipt from the recipient. Enquiries

go no further; the expenditure of the grant is not in general followed by the Comptroller and Auditor General, nor is the recipient required to surrender an unexpended balance. In the case of grants in aid of Colonial revenues, the Colonial Office does in fact keep a close watch over the expenditure, and audits it by an audit-staff of its own. But that is a matter of domestic administration at the Colonial Office; it is no part of the Parliamentary scheme of audit and appropriation. The only duty of the Comptroller and Auditor General in respect of the grants is to see that the Accounting Officer, whose duty it is to pay them over to the recipients, produces a receipt for their payment.

Grants in aid serve a useful purpose. They enable the State to help an object without becoming responsible for it. But they make a hole in the defences of the scheme of appropriation, and so they need, and receive, careful watching by the Public Accounts Committee. They are legitimately applicable to those objects only which are beyond dispute objects for which the State should not make itself directly responsible. By extending them to objects for which the State is or ought to be responsible it would be easy for a minister or a department to withdraw an increasing amount of expenditure from the control of Parliament.

## Payments to Local Taxation Account

It is convenient to deal here with another sort of expenditure that escapes the control of appropriation and audit. Parliament does a part only of

the work of government: another part is done by local authorities. They have their own local revenues, the rates, out of which they meet their expenses. The work which they do is for the most part local work, and properly paid for out of local contributions. But in part also it is not local work but national, to which it is proper that a contribution should be made out of the national revenue raised by taxes. In recognition of that, Parliament helps the local authorities by paying them certain sums every year out of the Exchequer. These are called payments to Local Taxation Accounts. They are a Consolidated Fund Service, made on the authority of standing Acts of Parliament and not voted afresh every year. Their amount has been fixed in no very scientific way. From time to time, as Parliament has imposed fresh taxes, it has set aside a part of them for the Local Taxation Account, so that the amount now depends on a number of statutes making special allocations to the Account out of various sources of revenue. By the Finance Act of 1909–10 and the Revenue Act of 1911 the principal amounts to be allocated, which before were variable, became fixed, so that now the amount of the payments changes little from year to year. Formerly the amount due to the Local Taxation Accounts were not paid into the Exchequer Account at all; they were paid over directly to the Local Taxation Account by the Revenue departments out of the revenue as they collected it. A large part of the revenue was thus withdrawn altogether from the control of Parliament, and for that reason an end was put to the arrangement by the Finance Act of 1907. Since that time the part of the revenue due to Local Taxation Accounts with minor exceptions has been

paid into the Exchequer Account, and the contributions to the Accounts have been charged upon the Consolidated Fund. That circumstance has to be borne in mind in comparing the total of national revenue and expenditure before and after the financial year 1907–8. Before that year Exchequer issues and receipts did not include contributions to the Local Taxation Account; after it they do, and are the greater in consequence. In the Statistical Abstract and in other Returns which show the comparative total of revenue and expenditure from year to year a correction is made in respect of the change in order to show the true comparison. The payments of the contributions to the Local Taxation Accounts out of the Consolidated Fund are audited by the Auditor General as payment on account of any other Consolidated Fund service is audited. Further he is not concerned with them, nor do they enter further into the national system of accounts. They pass into the hands of local authorities as grants in aid do when they are paid to their recipients.

Such is the nature of the appropriation audit made by the Auditor General under the Exchequer and Audit Acts and his other powers. It is claimed, and no doubt with truth, that every irregularity which in former days would have been judged and buried within the walls of a department is now examined and reported on, and is thus subjected to public criticism.[1] Misapplication under the existing system is difficult, and overdraft, it is said, is impossible. It is common indeed to attach an almost superstitious reverence to the system, and to speak of it as if it were the grand bulwark of

[1] Treasury Minute, 4800/76. 20/3/1876.

economy against the inroads of all sorts of waste and extravagance. Without in any way belittling its importance, we must face the fact that it is nothing of the sort. Waste and extravagance the Appropriation Audit does not even set out to hunt: its prey is illegality, and there are countless ways of wasting public funds with every circumstance of legal sanction. When the Auditor General has discovered and reported upon every case in which money has been appropriated by the departments otherwise than as directed by Parliament, he has fulfilled his statutory functions. Were we to look to his Appropriation Audit for defence from extravagance, for a check upon increasing estimates, or for assurance that public money is being spent to the best purpose on the services to which Parliament has appropriated it, we should be looking to it for something which it cannot do and is not intended to do. Its purpose is a different one and one easier to achieve, although not less necessary. It secures the control of Parliament over its grants after they have passed out of the hands of Parliament, that and nothing more; and the taxpayer must seek elsewhere for a defence against legal waste and inefficiency in expenditure.

## Administrative Audit

He will find it in some measure in certain inquiries made by the Auditor General which arise out of the work of the Appropriation Audit but are not necessary to it, and for the making of which he has no statutory authority. As said, it is with the regularity of payments that the statutory appro-

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[1] Treasury Minute, 4800/76. 20/3/1876.

technical, this administrative part is of the highest practical value as a remedy for the epidemic complaint of financial administration in these days of vast expenditure, neglect of rigid economy in details. To illustrate its value two examples may be quoted, one great and one small. It was an inquiry and report by the Auditor General on improprieties obvious on the face of the accounts submitted to him that brought to light the irregular transactions in connection with the disposal of army stores after the South African war. He found simultaneous contracts made by the military authorities with the same parties for the sale of hay and so on at a lower price and for its purchase at a higher price, a process which, as common sense could tell, needed some apology. His report to Parliament upon these irregularities led to the appointment of a Royal Commission and to the reorganisation of the system of military administration. In another case the Auditor General found that a department had ordered some ribbon from a contractor at fourteen shillings, had cancelled the contract, and had then given a fresh order for the same ribbon at twenty shillings. There might be an explanation, but an explanation was certainly needed. He asked for it and was refused, and reported to the Committee. The Committee supported his action, the Treasury told the department that he was more than justified, and this now stands as the leading case in support of the Auditor General's right and duty to make inquiries into administrative matters of the sort, even outside the sphere of his strict statutory powers.[1]

[1] Second Report, Public Accounts Committee, 1888, and T. M. thereon.

Great as is the value of the administrative part of the Auditor General's audit, it is clear that it must be very limited in its scope. Such loss and wastage only can come to his notice as are patent on the face of the accounts and documents submitted to him, and it is an incautious department that allows its accounts to go forward with patent defects of the sort clamouring for inquiry, when by any means it can eliminate them. Lack of intimate knowledge of the methods of the departments, and especially of all those technical affairs with which the Admiralty and War Office are concerned, must greatly impede him in his researches. It can only be a few of the most obvious and not always the most grave cases of waste that an officer in his position can hope to discover. His inquiries moreover come after the event, and although it is better that they should come then than not at all, it is better still when the check on waste comes before the waste has been made. If the public is to have the protection of a full and prompt administrative audit, made with intimate knowledge of the work of the departments and with better means of information than accounts and documents carefully prepared for the inspection of an external examiner, it must get it in another quarter and that is in the financial branches of the great spending departments themselves. An internal administrative audit is in fact being continuously conducted by those branches in the better organised departments, and where it is not it ought to be.

With the growing volume, elaboration, and technicality of the work of government, it is to the expert and semi-independent financial branches of the great departments that the public must look for

its substantial protection against waste and loss. External and therefore comparatively inexpert guardians, such as the Auditor General, the Public Accounts Committee, and the Treasury, high as the value of their work undoubtedly is and essential in the legal scheme of Appropriation, in the practical matter of enforcing economy in administration can only supplement the work done within the departments themselves. So vital have the services of the financial branches of the great departments become to the cause of economy that it is to be wondered at that their organisation and conditions of labour are left to the uncontrolled discretion of the ministers and the Executive. A minister can make what he likes of his financial branch; he can make it an efficient and active body under the conditions described, or by segregating it, by subordinating it to the executive officers, and by confining it to the mere routine of accountancy, he can reduce it to impotence. Parliament has hedged about the powers and independence of the Comptroller and Auditor General with all the protection that Acts of Parliament can give. Now that the cause of economy must depend even more on the financial work done inside the departments, if there is to be any advance in the direction of strengthening financial control it must be by extending something of the same protection and security to the financial branches, as much of it as is consistent with maintaining unimpaired the ultimate responsibility of the supreme head of the department.

# CHAPTER VII

## APPROPRIATION: TRANSFER AND EXCESS

Parliament, in the Appropriation Act which completes its financial labours for the year, lays down a cut-and-dried scheme of expenditure for every service in every department throughout the year. Votes are the lengths into which it cuts the scheme of appropriation to dry it. Each specifies a service or a group of services and grants a sum therefor. Parliament says to the department in the Act, "Here is the amount which you are authorised to spend on each Vote; you must not spend more nor must you spend money granted to you for one Vote upon another for which it was not granted." A Vote and its grant are water-tight. It will be remembered that the grant of Parliament on each Vote is a net grant; it is equal to the gross sum estimated to be necessary during the year for the services included in the Vote, less the minor receipts which the department estimates that it will collect during the year in connection with those services, and which Parliament authorises the department to appropriate in aid of its estimated gross expenses. To avoid a possible mistake it will be useful to remind ourselves here of another circumstance. Owing to the fact that the Paymaster General keeps a general balance and not a special balance for each Vote or even for all the Votes of each department, credit

issued from the Exchequer for the spending departments, although it is specified to be on account of a particular Vote, is not earmarked in the hands of the Paymaster General for the Vote on account of which it is issued; it is drawn upon for any Vote on account of which payments may legitimately be made. There is thus a sharp distinction between issues and grants. As a matter of banking, once an issue of credit from the Exchequer is merged in the Paymaster General's balance, it is as impossible to follow and earmark as a lucky sixpence which an old lady pays into a bank. It can be used for any Vote. But as a matter of account, money granted for one Vote may not be accounted for on another. What is meant when it is said that a Vote and its grant are water-tight is that at the end of the year or at any other intermediate season at which it is thought useful to adjust the Vote Accounts, the department must show that no more has been spent on each Vote than Parliament has granted for it. It must not in the first place spend more than the total amount which it has to receive and so run itself into debt; that is the highest crime and misdemeanour of all. Further, even though it has received more in respect of minor receipts than it estimated that it would receive, it must not take advantage of that to spend more in gross upon its services than is authorised in the Appropriation Act, even though it would not, under the circumstances, run into debt. It is authorised to appropriate in aid of its expenditure the amount specified in the Appropriation Act, and no more. These rules apply to the total of its grants, and they apply to them also Vote by Vote. A department must not overspend one Vote, and avoid running into debt,

by transferring to the overspent Vote credit which has been saved upon another. In accounting for its expenditure it must show, Vote by Vote, that no more has been spent on the services included in each out of Exchequer issues, and that no more has been appropriated in aid of them out of minor receipts, than the Appropriation Act authorised. This rule of the water-tightness of the Vote is that which underlies the whole system of accounting, and the various details of the system, with which we have now to concern ourselves, can best be understood as modifications of the rule, and as exceptions.

In the Appropriation Accounts, which follow the form of the estimates, Votes are grouped in classes and subdivided into sub-heads; but it is the Vote that is the water-tight unit, not the sub-head or the class. A department may save money on one sub-head and spend it on another. When the public service requires it, the details of the sub-heads may[1] thus be varied and credit may be transferred from one to another within the limit of the total Vote. To do so, the sanction of the Treasury is needed, and in the case of the Civil Service estimates the Treasury sees that it is obtained. In the case of Navy and Air Votes, the sanction of the Treasury for such transfers is little more than a formality, unless the transfer involves some question of principle or of change of policy. In the case of some Votes, there is a still more minute division of the form of the Vote into subdivisions of sub-heads; but these are merely explanatory; they do not limit appropriation and the leave of the Treasury need not be obtained, in

[1] But see footnote [1] on p. 164.

any case, to spend upon one money saved upon another.[1]

There is a good reason for allowing to the departments this power of transfer within the limits of the Vote. If they are allowed to enjoy the benefit of a saving on one sub-head to cover a deficiency on another, they have a motive for economy. Were the power to be denied them, it would tend to make them over-estimate every sub-head in order to avoid the danger of a deficiency on any. It would have another ill effect also; it would make a much greater number of Supplementary Estimates necessary to authorise unexpected increases of expenditure. The need for Treasury sanction is an adequate check to prevent the abuse of the power, and the Treasury's exercise of its power is itself subject to the criticism of the Auditor General and of the Public Accounts Committee.

## Overspending

Absolute rigidity in the scheme of appropriation by Votes is the ideal, but it is an ideal not to be attained in a world of surprises, and owing to unexpected increases in the expenditure or unexpected deficiencies in appropriations in aid, Parliament commonly finds it necessary in practice to make some provision for alterations and additions to the scheme during the year, to provide for overspending of the Votes. It does so in the first place

[1] There are some exceptions to this rule, of cases in which Treasury sanction is needed for an excess upon an item in the estimates, although that would not lead to an excess upon the whole sub-head. They are cases of new expenditure which would tend to increase charges permanently. For example, Treasury sanction is needed for an excess in respect of extra clerical assistance.

by Supplementary Estimates, those necessary evils. By their means provision is made for the chief additions to expenditure which are found to be unavoidable. After presentation they pass through all the stages of procedure through which the original scheme of expenditure passed, and by their inclusion in the next Appropriation Act they are grafted on to the general scheme of appropriation. Grants for services included in Supplementary Estimates have then to be accounted for in the same manner as those included in original estimates. Both are rigidly appropriated and both are subjected in appropriation to the limitations already defined, and to the exceptions with which we deal later. A Supplementary Estimate, it is to be observed, needs the assent of the Treasury as much as an original estimate. As soon as a department sees that probably it will have to spend in excess of the amount which it was authorised to spend, it is its duty to call the matter promptly to the attention of the Treasury. There investigations are made to see whether the call to excess expenditure is really so urgent as the department supposes, whether in particular by hook or by crook the expenditure cannot without detriment to the public service be postponed to the coming year, so that it may be included in that year's ordinary estimates. If it cannot, the Treasury authorises a Supplementary Estimate, and in making it up credit is given for any excess in the Appropriations in aid of the department's Votes over those originally estimated. It may be that the excess in appropriations in aid is so big that it is enough to meet the whole of the excess expenditure. All the same, since the department cannot appropriate in aid more than it was authorised

so to appropriate, a Supplementary Estimate is necessary.[1] It is drawn up so that there is a nominal excess of £10 or £100 or so of excess expenditure over additional receipts, and that nominal sum is voted by Parliament, so that the matter may be brought into the structure of the scheme of appropriation. As soon as a Supplementary Estimate has passed safely through Committee of Supply, the service for which it provides may be financed out of any Ways and Means already granted, but not appropriated,[2] and the department need not wait until the supplementary provision has been included in a Consolidated Fund Act. Sometimes, however, it becomes necessary to incur expenditure on an unforeseen service when Parliament is not sitting, or otherwise before a Supplementary Estimate can be presented. In such a case the Treasury, if it is convinced that the necessity is real and urgent, takes the responsibility of authorising the department to "proceed in anticipation of Parliamentary sanction."

If events involving additional expenditure unforeseen in the original estimates happen so soon, as they sometimes do, that when they happen the Vote for the service affected has not yet been taken in the Committee of Supply, it is possible to avoid a Supplementary Estimate altogether. All that is then needed is that the Minister responsible for

[1] Similarly, if the new service is one which in the opinion of the Treasury ought not to be begun until Parliament has approved it, a token Supplementary Estimate is taken, even if sufficient savings are available on the Vote.

[2] Public Accounts and Charges Act, 1891, § 2 (1). Where an Act authorises any sum to be issued out of the Consolidated Fund towards making good the supply granted to Her Majesty for the service of any year, every sum issued in pursuance of that Act shall be applied towards making good the supply so granted *at the time of such issue.*" (See also p. 122.)

the Vote should withdraw the original estimate therefor and substitute a new one to meet the altered circumstances, or that he should simply lay a statement before the House of the additional expenditure to be voted.[1]

### EXCESS

Changes in the original estimates before they are voted make a difference in the ultimate scheme of appropriation, and Supplementary Estimates make additions to it; but it is to be observed that both are embodied in it and are no exceptions to the rule that the scheme is invariable. In the case of the Civil Departments, that rule holds absolutely. They have no authority to vary the cut-and-dried schedules for the Civil Service Votes in the Appropriation Act, and nobody has any power to give them such authority. In their case, therefore, it remains only to consider what is to happen if, as the year draws towards its close, and it is too late to present a Supplementary Estimate, it is found that some negligence or perhaps some unavoidable mistake has led a department into overspending itself in a manner unforeseeable perhaps and at any rate unforeseen. It is not until some six months after the close of the financial year that the Appropriation Accounts are made up and audited, and that is the time at which regrettable incidents in the way of unforeseen and unauthorised overspending of Civil Service Votes will in general come to light. There can then be no more Supplementary Estimates

[1] In the case of Navy and Air Votes, in conformity with the practice explained later in this chapter, if it is already apparent that there will be savings on other Votes of the same department, a minute is presented at this stage to specify them and to show how they will cover the additional expenditure.

for a year the accounts for which are closed, so some other steps have to be taken. Excess expenditure of the sort is brought to the light of day by a special entry which has to be made in the Appropriation Account of the department concerned, and by the report of the Auditor General thereon to the Public Accounts Committee. The first step usually taken is for all parties concerned, the Auditor General, the Public Accounts Committee, and the Treasury, to remind the peccant department that it is a canon of the public service that an excess of the sort is a financial offence, and that it would do well to read the Resolution of the House of Commons of March 30th, 1849, that: "When a certain amount of expenditure for a particular service has been determined upon by Parliament, it is the bounden duty of the department which has that service under its charge and control to take care that the expenditure does not exceed the amount placed at its disposal for that purpose." After some such suitable admonition, the Executive and the Legislature dry their eyes and set to work to mop up the spilt milk. Parliament has formally to regularise the excess. For that purpose, after the Public Accounts Committee has reported on the cause and cure of the administrative ailments that led to it, a resolution is proposed in Committee of Supply, authorising the application to meet the excess of any savings that have been made on other Votes and the appropriation in aid of it of any minor receipts in excess of the estimated receipts already appropriated. It is in most cases out of these extra receipts that the excess expenditure has already been met by the department, so that the resolution only regularises accomplished facts. After being passed in Committee

of Supply, the resolution goes through all the numerous stages of ratification which every resolution for the expenditure of money has to go through, and finally, and before the end of the year, it gets the force of law in the Consolidated Fund Act, and credit to cover the excess is issued to the department from the Exchequer. The grants are appropriated in the next Appropriation Act. It will be observed that the issue from the Exchequer thus takes place at the end of the year following that during which the excess expenditure was incurred, and the appropriation is not made until well on in the financial year following that again.

### TRANSFERS ON NAVY AND AIR VOTES [1]

Thus in the case of Civil Service Votes expenditure unforeseen in original estimates is dealt with by Supplementary Estimates; and any excess expenditure unauthorised by a Supplementary Estimate is regularised by an Excess Grant. Navy and Air Votes stand on a different footing. Admiralty and Air Ministry have far more to spend. Civil expenditure is for the most part of a routine sort: the expenditure of the Admiralty and Air Ministry is that of great manufacturing and contracting businesses which are big employers of labour and buyers and sellers of goods. They have markets to study, those uncertain things, and are less able than the Civil departments to

[1] This section does not apply to Army Services, for which, as we have seen, there is now a single Vote. But the War Office have informed the P.A.C. and the Treasury that they will conform to the old practice, which was identical with that here described in respect of Navy and Air Votes; i.e. that they will for this purpose treat the Heads of the Army Vote as if they were separate Votes.

foresee exactly what they will have to spend and when. For those reasons it is impossible to tie them down so rigidly to their Votes. Parliament does not attempt to do so: it exacts from them a less precise obedience to its scheme of appropriation. Supplementary Estimate and Excess Grants may be made use of for the Naval and Air Votes as for the Civil, but a certain freedom is allowed to the Admiralty and Air Ministry to disregard the theoretical water-tightness of the Votes which makes an excess grant, at least, seldom necessary.

The rule that the total of the grants to the Admiralty and Air Ministry respectively must not be overspent is enforced with absolute rigidity. If the melancholy fact becomes apparent that that total will be insufficient for either department, it must take steps to obtain a Supplementary Estimate. But into the instrument by which Parliament defines its scheme of appropriation, the Appropriation Act, it slips a provision which gives the two departments a large measure of liberty to readjust expenditure within the limit of the total sum granted to each. Civil departments, it will be remembered, are allowed with Treasury sanction to transfer the savings on one sub-head of a Vote to meet expenditure on another sub-head. Admiralty and Air Ministry are allowed to make similar transfers from Vote to Vote. A section found in every Appropriation Act, year by year, provides that: "(1) So long as the aggregate expenditure on naval and air services respectively is not made to exceed the aggregate sums appropriated by this Act for those services respectively, any surplus arising on any Vote for those services, either by an excess of the sum realised on account of appropriations in

aid of the Vote over the sum which may be applied under this Act as appropriations in aid of that Vote, or by saving of expenditure on that Vote, may, with the sanction of the Treasury, be temporarily applied either in making up any deficiency in the sums realised on account of appropriations in aid of any other Vote in the same department, or in defraying expenditure in the same department which is not provided for in the sums appropriated to the service of the department by this Act, and which it may be detrimental to the public service to postpone until provision can be made for it by Parliament in the usual course.

"(2) A statement showing all cases in which the sanction of the Treasury has been given to the temporary application of a surplus under this section, and showing the circumstances under which the sanction of the Treasury has been given, shall be laid before the House of Commons with the appropriation accounts of the naval and military services for the year, in order that any temporary application of any surplus sanctioned by the Treasury under this section may be submitted for the sanction of Parliament."

In a field of expenditure so wide as that in which the Admiralty and Air Ministry move, savings in one region or another are sure to be made. All then that the department in question has to do when it finds that overspending of some Vote is inevitable is to look around for some equivalent or greater saving on some other Vote, and to get leave from the Treasury to meet the overspending out of the saving. No Supplementary estimate is necessary, and no excess grant, as long as the total of the department's grants is not overspent.

It will have been noticed that according to the wording of the Act the savings may, with the sanction of the Treasury, be applied to the deficiencies temporarily. That does not mean that the savings are ever repaid; what it does mean is that the Treasury's sanction is not final, and that the ratification of Parliament must be got for it before the end of the financial year. Things take the following course. As the year draws towards an end and the Admiralty and Air Ministry begin to see how they stand as regards expenditure, they tell the Treasury of the excess expenditure that there will probably be on some of their Votes and of the surpluses on others. They send to the Treasury a schedule of the items of excess expenditure and surplus, made out in detail, Vote by Vote, with explanations. Surpluses may be the result of a saving on the total expenditure estimated for a Vote, or of bigger receipts for appropriation in aid than those allowed for in the estimates; and conversely excess expenditure may be the result of a total expenditure on a Vote greater than that estimated, or of a disappointment in respect of appropriations. Authority to make the transfers is then given by the Treasury under the power given to it by the cited clause in the Appropriation Act. It sets out in detail in a minute the probable excess over grants, Vote by Vote, sets against the excesses the probable surplus in a lump, and authorises the temporary application of the one to meet the other.[1]

A copy of the minute is laid before Parliament before the end of the financial year, and there

[1] Sometimes the Treasury sanctions an excess conditionally, subject to a surplus being subsequently realised on another Vote.

the matter rests for a space. It is the Appropriation Accounts that bring it again to the light of day. Their chief end and object is to show how far the departments have kept to and how far they have strayed from the scheme of Appropriation. Above all things, therefore, they must show on the face of them the excesses and surpluses with which we are dealing, and how one has been applied to meet the other. In his scrutiny and audit it is the duty of the Auditor General to make sure that Treasury authority has been obtained for all such transfers, and the Public Accounts Committee takes retributive action if he reports that it has not been obtained. When the Public Accounts Committee has examined into and reported on these matters, the transfers are ripe for their final authorisation by Parliament. The House of Commons resolves itself into a Committee of the whole House on Navy and Air expenditure. A Resolution is presented to it, for instance, "that whereas it appears by the Navy Appropriation Account for the year ending March 31st, 1922, that the aggregate expenditure on Navy Services has not exceeded the aggregate sum appropriated for those services, but that the total difference between the Exchequer grants for Navy Services and the net expenditure are as follows:—

| | £ | s. | d. |
|---|---|---|---|
| Total Surpluses (on Votes) ... ... | 8,726,244 | 16 | 4 |
| Total Deficits ... ... ... ... | 1,268,386 | 3 | 6 |
| Net Surplus ... | 7,457,858 | 12 | 10 |

and whereas the Treasury has temporarily authorised the application of so much of the said total surpluses as is necessary to make good the said total deficits, the application of such sums

be sanctioned." After being passed in Committee, the resolution is reported to the House. Finally it is incorporated as a clause in the next Appropriation Act, which gives it the force of law, and there is annexed to it a schedule setting out the details of the deficits and of the surpluses apportioned to meet them, Vote by Vote. Thus the transfers receive at least a posthumous incorporation in the scheme of appropriation. Since the House waits for the Appropriation Accounts before it deals with the matter, the incorporation does not come until long after the transfers were made and approved by the Treasury. For instance, the transfers referred to in our example were those shown in the Appropriation Accounts for the year ending March 31st, 1922. That means that they were sanctioned by the Treasury in that month. But since the Appropriation Accounts for that year are not presented to Parliament until the beginning of the session of 1923, the transfers cannot be dealt with in the Appropriation Act of 1922 and have to wait for that of the following year.

Such is the course by which excess expenditure on Naval and Air Votes is set off against savings, within the limit of the total grants to each department. If the Appropriation Accounts show that either department or the War Office has exceeded its total grants, then, as in the case of a Civil department, there is nothing for it but an Excess Grant. The Public Accounts Committee is careful to report upon any case, Civil, Military, Naval, or Air, in which a Vote for an Excess Grant is required, in time to enable the Vote to be passed by the House before the end of the financial year following that in which the excess expenditure was made. As in

the case of the Civil departments, against Naval, Military, or Air excess expenditure is set in the Excess Vote any surplus in appropriations in aid over that allowed for in the estimates and original Appropriation Act.

Power to make transfers is subject to certain temptations, and no suitable control that can be exercised over it is unnecessary. It tempts those responsible for the preparation of the estimates to over-estimate the expenditure to be required on certain Votes, in order that the grants for those Votes may be used as a pool to draw upon for other Votes. When it is found that a certain Vote is in fact constantly being over-estimated and showing big savings, a critic may suspect that the department is regarding it as a milk-cow for its other Votes. It needs no argument to show the impropriety of a practice of the sort. In plain words, it is deceiving Parliament; it conceals from it at the time at which it is considering the estimates the true intentions of the department, and enfeebles Parliamentary control. On the other hand the existence of the power of transfer, legitimately used and subject to proper limitations, makes for accuracy in estimating and for economy in expenditure. That has already been pointed out in connection with transfers between the sub-heads of the Votes of the Civil departments. It is equally true of transfers between the Naval and Air Votes, and between the Heads of the Army Vote. Without the liberty to transfer, the Admiralty and Air Ministry would be tempted to over-estimate every Vote in order to prevent the possibility of troublesome excesses, and they would not have so strong a motive for making savings.

Another specific temptation to which the power of transfer subjects a department is the temptation to invent something to do with savings when it finds that it has some, whether that something is really necessary or not, just in order to find a use for the money. Obviously the Treasury ought to be, and no doubt it is, on the *qui vive* to prevent so extravagant a practice. On the other hand, if a department does happen to have savings in hand at the end of the year, it may be that the state of one or other of the markets in which it buys goods for the public service may make it very desirable, in the interests of economy, that it should make use of its savings in buying at once for its requirements in the coming year. It may not be in any sense necessary that it should do so, and yet it may be quite prudent that it should; and under those circumstances the Treasury will in general make no objection to the department looking round and seeing whether it cannot make an ultimate economy for the taxpayer's pocket by using up its savings.

# CHAPTER VIII

## THE ANNUAL BALANCING

We have had a good deal to do in the pages that have gone before with the Exchequer Account. The importance of this, the account of the Consolidated Fund of the United Kingdom, is so great that its nature and incidents should now occupy us in more detail. We have seen how, in theory, it is the account which receives the whole of the nation's revenue, and out of which the whole of the nation's expenditure is made; and we have noticed several substantial exceptions to the rule, such as the sums retained as Appropriations in Aid and for the expenses of the Revenue departments. We have seen how at ordinary times the use for payments by the Paymaster General of credit from his general cash balances prevents any exact correspondence between issues from the Exchequer Account and the nation's actual expenditure, and how in the same way the retention of revenue for the expenses of the Revenue departments prevents any exact correspondence between Exchequer receipts and the nation's actual revenue. We have seen also how the periodical adjustment of Vote Accounts makes Exchequer Issues and Receipts roughly equal, and at the end of the year equal with tolerable accuracy, to the total of the nation's incomings and outgoings.

## The Exchequer Account

Thus the taxpayer has in the Exchequer Account a guide to the state of the public purse. He is enabled to follow it from week to week in a return published by the Treasury in the *London Gazette* every Tuesday, a summary of which is given in the financial columns of most of the newspapers. On one side are shown the total receipts into the Exchequer Account, from the beginning of the year, in comparison with those for the same part of the preceding year and with those estimated for the whole year. Receipts are distributed under their headings of Customs, Post Office, and so on, and receipts on capital account are stated separately. On the other side is shown the expenditure since the beginning of the financial year, compared as in the case of the revenue, and distributed under the headings of Debt Services, Development and Road Funds, Local Taxation Accounts, other Consolidated Fund Services, and Supply Services. Issues on capital account are stated separately. Finally the amount of the balance in the Exchequer is stated, and compared with that at the corresponding period of the year before. By deducting from the totals of revenue and expenditure at the end of any week those at the end of the week before, one can see what has happened during the seven days in between. Once a quarter the Treasury publishes a fuller record of its dealings with the Exchequer Account. It is divided into two parts, the first of which shows with a little more detail than the weekly account the revenue received into the Exchequer Account, both for the quarter and for the whole financial year up to the date of the return, in comparison with

that for the corresponding periods of the preceding year. In the second part receipts into the Exchequer Account, including receipts on capital account, are set against expenditure, including expenditure on capital account, and a balance is struck which is the "balance in the Exchequer." At the end of the financial year the weekly and quarterly returns are developed into the Finance Accounts of the United Kingdom of Great Britain and Ireland, which make their appearance some time in June in the shape of a blue pamphlet, which every taxpayer ought to buy, read, and inwardly digest.

At the end of the financial year, as the clock strikes four p.m. on March 31st, the Exchequer Account for the year is closed. During the preceding weeks the departments have been obtaining from the Treasury issues from the Account calculated to make the total issues which they have received equal to their actual expenditure, thus repeating with increased precautions the process gone through at the end of the three intermediate quarters. On March 31st in consequence the receipts into the account and the issues therefrom correspond to a very close degree of approximation with the whole of the nation's incomings and outgoings for the year. Nevertheless they are not identical. A record of issues from the Exchequer is always a record of imprests, or payments to the department as agents on account, to be disbursed by them for the Government. It never is nor can be a record of actual expenditure in the form of final payments. Owing, however, to this balancing of the Accounts of each Vote, by special issues made in March, and to the policy which keeps free balances in the hands of the spenders as low as possible, for all practical

purposes the anxious and curious taxpayer can look upon the record of receipts and issues from the Exchequer during the year as the record of the Government's actual revenue and expenditure, and it is that which he finds in the Annual Finance Accounts. He finds there the nearest approach which the Treasury can provide to the general account of outgoings and incomings for the preceding year which the prudent householder prepares for himself in those grim days of reckoning that follow Christmas and the New Year. As every citizen is part holder in the house of the state, each is equally concerned to study the record of the incomings and outgoings of those who manage his house for him, which they set down so conveniently in black and white and sell to him at two shillings.

A look at the chief figures of the record of the Exchequer Account for the year is all that is needed to get a general idea of the state's getting and spending; but to get an exact idea of what the Account does show and what it does not, it is useful to study with more attention the conditions under which it is made up at the end of the financial year, at four p.m. on March 31st.

## The Cash Account System

In the first place, it should be noticed, the Exchequer Account is a cash account. It shows receipts and issues actually made during the year, not, as it would under some continental systems of state accounting, rights accrued and liabilities incurred. Liabilities appear on it only when they are met by issue to the actual spenders, not when they are

incurred; and revenue when it is received, not when it is due. This is a principle that is applied also in every other account that is related to the Exchequer Account and in particular to those of the great Spending and Revenue departments. Revenue departments must bring into account as revenue belonging to the year only such revenue as was actually received during the year. They must not include revenue which was due but was not actually received. Similarly spending departments may bring into account as chargeable against the grants of the year only those payments which were actually made during the year. They do not include payments for which they became liable but which they did not actually disburse. In the continental systems referred to every liability is brought into the accounts for the year that is incurred therein, although no payment is made for it until long after, and similarly all revenue is brought into account that ought to have been received, although it may not have been received in fact. In the result, when the financial year ends, it is still quite uncertain what the realised total of the expenditure and revenue which are considered to belong to the year will be, and the nation's accounts for the year have to be kept open long after the year is over. From that result great uncertainty and confusion. It makes it impossible to determine before embarking upon the finances of the succeeding year how those of the preceding year have turned out; and obviously it is useful to know where you are before you set out on a fresh voyage. Theoretically the continental system is better, if it be considered that it is of first importance to treat fiscal operations as having a specific character of their own simply because they

take place in one year rather than in another, and to find out exactly what the result of each year's fiscal operations is, as distinguished from those of any other year. But it is difficult to see any good reason why the fiscal year, as such, should be endowed in this way with a character and personality. The business of Government is continuous, and there is no special interest or value in undertaking laborious investigations and adjustments in order to allot to a certain year or to any other fixed period all the operations which can theoretically be considered to have had their origin therein. What is of value is that the accounts should be nipped off sharply on a fixed date and a balance struck, in order that the Chancellor of the Exchequer may be able to start fresh on his budget with exact knowledge of the nation's financial position. This our system of cash accounts enables him to do. By considering only the realised receipts, and the realised expenditure (by way of imprests to spending departments), and by disregarding debts which may turn out good or bad and liabilities which something may yet happen to increase or diminish, the Treasury is enabled to close the Exchequer Account immediately the year ends on March 31st. It is enabled on the same evening to make a statement of its position which shows not exactly indeed but to a very close degree of approximation the whole of the nation's revenue and expenditure for the year and the difference between the two at its close, surplus or deficit. If there is a surplus of revenue for the year over the expenditure charged against it, it is not left at large. As we shall see in a later chapter, at once at that time and on that day it is set to a separate account, which is the

account of the Old Sinking Fund for the reduction of the National Debt.

Since issues from the Exchequer Account are imprests and not final payments, at four o'clock on March 31st the money which the Government has is in several hands. There is a balance on the Exchequer Account, safe under the thumb of the Treasury; but there is also a balance of issues from the Exchequer outstanding in the hands of the Paymaster General, and other balances in the hands of local paymasters as sub-accountants, who have received them as imprests from the departments which they serve. For the purpose of determining the revenue and expenditure for the year, outstanding balances are disregarded: having been issued from the Exchequer Account, they are treated as if spent. Thus the return of the Exchequer Account at the year's end shows as spent a certain amount of money that is in fact still in the hands of the Paymaster General and local paymasters. In the same way it fails to show as collected a certain amount of revenue that is already in the hands of the officers of the revenue departments. The account is cut off sharp on March 31st; but the business of government cannot be cut off sharp too. It has to be carried on continuously on the day of the closing of the national accounts just as much as on any other day, and that means that a certain amount of the revenue at the moment at which the account is closed is actually in course of transmission from the collectors to its bourne in the Exchequer Account. If the Government paid and received the same amount every day, year in, year out, there would be $\frac{1}{365}$ of the revenue received during each year accounted for in the next year,

and $\frac{1}{365}$ of the payments made in each year accounted for in the preceding year; and as the errors thus introduced would be equal and opposite in each case at the beginning and end of every year, it would introduce no total error into the balance between revenue and expenditure of each year as shown in the Exchequer Account. But since there is not that mathematical regularity in payments or receipts, either day by day or year by year, there is a slight error introduced into the accounts, sometimes one year getting a little help from its predecessor and sometimes the other way about. There is, however, a constant tendency for the two disturbances to accuracy, that at the beginning and that at the end of the year, to correct each other, and the error is quite small and unimportant in comparison with the total sums involved.

### Short Issues

As we have seen, when the year is drawing towards its close at the end of March careful calculations are made of the issues to be made from the Exchequer on account of each Vote for the year, in order that the actual net expenditure chargeable against that Vote may be covered as exactly as possible by Exchequer issues. For that purpose information is obtained by the Treasury from the departments responsible for expenditure on the Votes of their probable requirements in respect of each. Now, the grant of Parliament in respect of each Vote is a maximum grant. As much as Parliament grants to a department for the Vote *may* be spent on the services of the Vote by the department, but there is no reason why it should

spend or the Treasury should issue to it the whole sum granted, if it can do with less. If the Treasury hears from the department the glad news that it is not likely to want for the service of the Vote the whole of the sum granted, it makes a "short issue," leaving a part of the grant standing to the credit of the Vote still unissued at the end of the year.

## Exchequer Issues and Audited Expenditure

We have now to draw a distinction which it is necessary clearly to grasp and constantly to bear in mind in order to follow the system on which the Government's accounts are kept. It is the distinction between the Account of the Exchequer for the year and the yearly accounts of the departments. The Exchequer Account, which shows approximately the Government's total revenue and expenditure for the year, is, as we have seen, on the issue side an account of the actual issues made as imprests to the departments from April 1st to March 31st. The date of an issue is the criterion of the year in which it is to be brought into account. In drawing up the accounts of their expenditure for the year, which are the Appropriation Accounts, the departments have no such simple criterion as to what expenditure is to be included. What has to be included is the total expenditure, made by the department, which is properly chargeable against the grants for the year. To determine what expenditure is so chargeable, the criterion to be applied is the date of the order for payment, so long as that order has actually come into the hands of the payee and has not remained lying in the office undelivered. An accounting officer, then,

must bring into account for a year all operative payments the order or cheque for which was dated within the year.

It can be seen in the proceedings of the Public Accounts Committee and the minutes of the Treasury that this is a rule which is liable to be manipulated in a manner that calls for vigilance on the part of the guardians of financial morality. If a department's grants are running out and it is pressed for money it is tempted to leave some of the liabilities which it has incurred during the year undischarged, and by refraining from making out an order for payment until after the fateful 31st of March to throw the charge upon the Votes of the following year. On the other hand, if it has a surplus in hand at the end of the year it is tempted to get the benefit of it, and to avoid having to surrender it in the manner to be described later, by spending it on services which could more properly be performed in the following year. To prevent these manipulations the Treasury and the Committee have laid down several supplementary rules. They have laid down a strict rule that payment for a liability is always to be made in the year in which it has matured and is due. Every liability for a payment which has matured must, when its discharge is postponed for lack of funds, be shown upon the face of the Appropriation Accounts. If there is no money to meet it, so much the worse. The irregularity, as the Committee tersely puts it, consists in incurring unauthorised expenditure in excess of the grants, and it is only increased by not defraying it.[1] Not even to avoid an excess is the discharge of a matured liability to

[1] Report of Public Accounts Committee, 1877.

be postponed. On the one hand, then, it is quite right for the departments to call in and wipe off all matured liabilities in the last days of March; but on the other hand it is quite wrong for them to extend that process to the inclusion of payments in anticipation of the next year's services, and the Treasury is concerned to see that no such raids are made by the departments upon their surpluses.

We are now in a position to understand a circumstance which often puzzles one who is examining the national accounts. It is that the total of the net expenditure included in the Appropriation Accounts and audited is never exactly the same as the total of issues from the Exchequer Account. Since issues from the Exchequer Account at the end of the year are made with the express purpose of balancing and exactly covering the actual expenditure of the departments out of the grants of Parliament, it seems as if the total net audited expenditure, which is the total net expenditure for which credit is taken in the Appropriation Accounts, ought to be exactly equal to the total issues from the Exchequer. So it would be but for one difficulty, that a certain number of cheques and orders for payment dated and sent to the payees in the last days of the financial year are not presented until after the end of that financial year on March 31st. When they are presented they are met out of the balances, in the hands of the Paymaster General and sub-accountants, part of which represents issues made in respect of the services of the year which is over. But it is very unlikely that the Treasury and the departments will have been able to foresee exactly and to a

pound how much will be required for these outstanding orders chargeable against the year. It may be that a little more has been issued than is ultimately needed, and in that case the Exchequer issues for the year will slightly exceed its audited expenditure. It may be that a little less has been issued than is ultimately needed, and then the audited expenditure for the year will slightly exceed its Exchequer issues. In the latter case the Treasury has to make fresh issues from the Exchequer in the new year on account of the services of the old, to cover the difference. They appear, of course, as part of the issues from the Exchequer brought into account in the new year.

It is now apparent why the departments' accounts of their expenditure, which are the Appropriation Accounts, cannot be made out at the same time as the final Account of the Exchequer for the year, as soon as the financial year is over. Time has to be allowed for the outstanding orders for payment chargeable against the grants of the expired year to be presented, to be met out of the outstanding balances issued on account of those grants, and for the expenditure to be audited. Payees are notoriously careless and dilatory, neglecting and forgetting to present their drafts for months and months. Some may never be presented at all. If after three months an outstanding draft has not been presented and met, no credit can be taken for it by the department which issued the draft. The payment will probably have to be made, but a new draft must be issued, and the charge will be against the Vote for the following year. After this period has elapsed, but not until then, the departments can set about the preparation of their Appropriation Accounts.

### The Surrender of Surpluses

In the last chapter we saw what is done when a department finds that it is going to spend or has spent more in gross upon a Vote than Parliament has granted to it for the purpose; but for simplicity's sake we left the converse case for consideration in the present chapter. It may be that when an Accounting Officer has made out the final account of expenditure on a Vote, he finds that less has been spent in gross upon the services of the Vote than Parliament granted for them. The surplus may arise in several different ways: it may be the result of the actual gross expenditure being less than the estimated gross expenditure, or of the realised appropriations in aid being greater than the estimated appropriations in aid.

That is for Civil Service Votes and the Army Vote. For Navy and Air Votes, owing to the system of applying the total savings on all the Votes to the total excesses thereon, the balance to be surrendered is the surplus of Supply grants over net actual expenditure for all the Votes taken *en bloc*. In either case if the whole of the grant or grants on which the surplus arises has been issued, then the whole of the surplus is in the hands of the department, and is represented by balances in the hands of the Paymaster General and sub-accountants. But if the surplus has been foreseen and the whole of the grant has not been issued, if there has been a short issue, then part of the surplus is represented by an unissued balance in the Exchequer Account.

A department which has effected a saving is not left in happy possession of it, to be spent upon anything it likes, as upon the services of the following year (which by the time the surplus is ascertained

is of course the current year). What it has saved, it has saved in the interests of the nation's common purse, and to that it must be returned. As for the surpluses outstanding in the hands of the departments, they might be returned by a transfer from the balances in the hands of the Paymaster General on account of the department to the Exchequer Account. But that would have one ill effect: it would increase the total receipts of the Exchequer Account and the total issues therefrom for the year by artificial cross-entries, and it would thus make both the nation's revenue and its expenditure seem bigger than they really were. A more convenient and a more scientific way of making the surrender is to let the department keep the surplus, but to reduce by an equal amount the grants to be made to it from the Exchequer for the services of the year following that to which the surplus belongs, thus reducing its potential credit on the Exchequer Account. The surpluses are then said to be written off the grants. That part of the surplus which is represented by grants still unissued from the Exchequer is written off and cancelled. It is only if a service has come to an end, no longer appears in the estimates, and all its grants for the past year have been issued, that a saving has actually to be paid back into the Exchequer Account as a receipt. One good effect of this system is that the use of the balances in the hands of the Paymaster General and sub-accountants which represent grants on account of the services of an expired financial year is not confined to meeting payments to be charged against the grants of that year. They are free to be used also for payments to be charged against the grants of the current year.

### Carry Forward and Reserve

By no well-managed business is the whole of its net income spent every year. If it is wise, it retains a part to provide for contingencies. In the case of a business concern the sum accumulated out of the net income to provide for contingencies is called the sum "carried forward," carried forward, that is, from the accounts of one year into those of the next. To that is sometimes added a Reserve Fund, which is a Fund consisting of savings out of income accumulated from year to year. Is there any Carry Forward or Reserve Fund in the accounts of the vast business carried on by the State? There are both.

Credit on the Exchequer Account is never exhausted when the financial year ends on March 31st. There is always a balance of unissued credit on the accounts at that time, called the Exchequer Balance, and that is the nation's Carry Forward. As we shall see in a future chapter on Sinking Funds, a part of that balance may, on March 31st, be automatically allocated to a certain specific purpose—the reduction of debt. It is the part which consists of the excess of the revenue for the year over the expenditure chargeable against that revenue. But there may be no such excess, and in any case it can only be a part of the Exchequer Balance. Nor is such excess necessarily paid out for the reduction of debt on March 31st: it is allocated to that purpose on that day as a matter of account; it is not issued as a matter of banking. The gross Exchequer Balance remains on the Exchequer Account, and is carried forward into the accounts of the ensuing year. If there is any deficiency in the year's revenue,

if it is less than the year's expenditure chargeable against that revenue, then the Exchequer Balance carried forward out of the year's accounts at its end is less than that which was carried forward into them at its beginning. To get a complete view of the record of the year's finance we must always have a look at Exchequer Balances at the beginning and end of the year. If that at the end of the year is less than that at the beginning, if, that is, the Government has reduced its carry forward, then it has not met the year's expenditure wholly out of the year's revenue, but in part out of the nation's permanent resources, of which its carry forward forms part.

For the nation's Reserve Fund we must look further into more obscure places. So far we have seen no sign of any in the national accounts. In all the accounts which we have considered hitherto, with the exception of the carry forward, everything is cut off sharply on March 31st: all outstanding balances are used up on one or another of the year's accounts and the accounts start absolutely blank for the following year. But if we look further afield through the accounts until we come upon certain two, called respectively the Civil Contingencies Fund and Treasury Chest Fund, we shall find what we are in search of, a diminutive but true reserve, balances which are not wiped out every year, but are continued from the accounts of one year into those of the next. They are not a general reserve; they are available for certain special purposes only. The purposes for which they are available are different, and we will consider them in turn.

## The Civil Contingencies Fund

In the course of the year the Civil departments often find that the rigid system on which their grants are appropriated confronts them with one or other of several difficulties. Either there is an urgent need that they should begin to provide money for some established service for which Parliament has not yet voted anything, or some wholly new and urgent little service turns up to be performed, for which Parliament has made no provision, or it becomes urgently necessary to overspend to a small extent the total Vote for a grant, and no excess has been received by way of appropriations in aid out of which, with the help of a Supplementary Estimate, to meet the overspending. Multifarious small payments have also to be made which are not appropriate to any Vote and are individually too small to be voted separately. Sooner or later Parliamentary authority must be obtained for all these small payments, and for any departure which emergency obliges departments to make from the scheme of appropriation; but meanwhile, what is to be done? To provide for such cases the Treasury keeps a nest egg in the form of a little loan-fund out of which it can make temporary advances to the Civil departments, and this is the Civil Contingencies Fund. It has a fixed capital which has been raised from time to time as the turnover of the Civil departments has increased. In 1913 it stood at £300,000, and in 1921 it was permanently increased to £1,500,000. A very large temporary increase in the capital of the Fund, to no less than £120,000,000, had been allowed in 1919, in order to enable it to finance through their last stages the big trading

services which had been undertaken by the State during the war. [The Vote of Credit, out of which these were formerly financed, came to an end with the war.] Out of the capital the Treasury makes advances to the Civil departments in anticipation of the grants of Parliament, when there is urgent need that payment for an established service should be begun before a grant is made. Advances of the sort are repaid to the Fund by the department when it gets its grant. Other advances are made to departments out of the fund to meet payments for small services for which Parliament has made no provision in the estimates of the year, and which cannot possibly be postponed until the next year. Others again are made to provide funds for such small overspendings of grants as the Treasury may agree to be inevitable. These last two forms of advance are repaid to the Fund out of grants of Parliament made specially for the purpose on Supplementary Estimates or Excess Grants. Thus the capital of the Fund is restored and maintained intact from year to year. At the financial year's end it is outstanding in the form of a balance in the hands of the Paymaster General, and it is carried forward into the new year to the account of the Fund. Owing to the wide powers of transfer between Naval and Air Votes, and the Heads of the Army Vote, the Admiralty and War Office and Air Ministry need no special machinery of the sort to enable them to deal with their similar emergencies. An annual account of the Fund is audited by the Auditor General and presented to Parliament through the Public Accounts Committee. The Commitee watches with some jealousy to see that the Treasury does not make use of the

Fund to release the departments to any substantial extent from the limitations of the scheme of appropriation.

## The Treasury Chest Fund

A purpose wholly different from that of the Civil Contingencies Fund is served by the Treasury Chest Fund. On the British Empire the sun never sets, and the British Government has to follow it round the world to make payments for the services which it requires in four continents and one continental island. Soldiers have to be paid and fed in a hundred scattered garrisons; warships have to be provisioned, coaled, and repaired, and the sailors paid, at a hundred naval bases, and civil staffs have to be maintained there to do the work. At Hong-Kong and Gibraltar the hand of the Government has to be as busy with disbursements as in Whitehall. There are payments to be made on account of the Diplomatic Service, and for pensioners resident abroad. In general the business of payment is administered at foreign stations in the same manner as at a home station. Imprests are issued by the departments to local paymasters (sub-accountants) in the form of orders upon the Paymaster General, for the use of which the local paymasters account. But there is an additional step that has to be taken in the case of payments abroad, and that is the transfer of credit to the foreign place at which it is to be used. An exchange is involved of the currency of one country for the currency of another. Even though the exchange is of sovereigns in London for sovereigns in Cape Town, owing to their distance apart sovereigns are very unlikely at any moment to

have exactly the same value in the two places, and so an exchange operation is in fact involved although the currencies seem to be the same. Exchange business of the sort involves some risk of loss: you may not be able to exchange a thousand pounds in London for a thousand at the Cape; you may be able to get only nine hundred and ninety-eight for them. It also takes time and locks up a certain amount of money in the actual course of transfer from place to place. But Parliament grants in general for the public services no more than they need, without allowance for the difficulties of transferring credit from place to place. Rates of exchange are as varying and unforeseeable as the wind. It would be impossible to estimate the allowance to be made for them beforehand, and wisely enough no attempt is made to do so. Yet if no provision were made for the matter, the departments involved would inevitably find themselves embarrassed by losing a fraction of their grants in transferring them abroad, and by always having a certain part of them locked up in the course of transfer. They might also be found bidding against each other in the exchange market, and so making the business more expensive for each other. To prevent that the Treasury keeps a special fund, and this is the Treasury Chest Fund. It is a little banking capital by means of which the Treasury carries on the business of exchange for the departments. Acting as banker for them, by the use of this fund, it makes good losses on exchange,[1] and provides the margin of money which is always locked up in the course of transfer.

[1] Not the whole of such losses, however; a part is provided for in the Votes, *e.g.* Vote II. of the Navy Estimates.

Since Civil Contingencies Fund and Treasury Chest Fund are often confused, we may take special notice of the differences between them. The Contingencies Fund is a loan fund for the use of the Civil departments at home; the Chest Fund is a banking fund for the use of the naval and military departments in particular, and always abroad. Advances from the Treasury Chest Fund can be made legitimately on the credit only of money actually granted by Parliament and available for repayment; advances from the Civil Contingencies Fund are never made on the credit of money actually available, but in anticipation of money to be granted later on. In one circumstance do the two funds resemble each other; out of neither must any final payment be made. Every payment made out of the Treasury Chest Fund, as out of the Civil Contingencies Fund, is repaid to it before the end of the year, and any loss of the capital of the fund in the course of the year is repaid to it by a special grant of Parliament. Thus the capital of the Treasury Chest Fund, as of the Civil Contingencies Fund, is maintained intact from year to year, and is carried forward undiminished at the end of the year to the accounts of the next year.

A special account of the fund, and its balance sheet at the end of the year, are audited by the Auditor General and submitted to the Public Accounts Committee. There is one possible misuse of the fund for which the Committee is on the look out. It exists for the purpose of laying down funds abroad, and they would be prompt to protest if the Treasury made use of it at home. It might thereby greatly loosen the bonds of the scheme of appropriation in which Parliament has confined

the departments. Any loosening of those bonds which is absolutely unavoidable is to be made by the use of the Civil Contingencies Fund under the prescribed limitations; and the Treasury Chest Fund is not to be used as a reserve to that.

## A Skeleton

We have now dealt with the system on which the nation keeps its accounts, in all its essential features. Before we leave it, it will be useful in aid of memory to turn back, to strip off detail and elaborations, and to arrange the bones of the structure into a skeleton.

The departments prepare Estimates, setting out what is to be done and the money to be spent in doing it, and dividing the services and the grants therefor into Votes.

Parliament considers and approves the Estimates, Vote by Vote, grants the money needed for each and appropriates it thereto, and provides for the raising by taxation of the money which it has granted.

The Revenue Departments collect the taxes for which Parliament has provided and pay them into the Exchequer Account.

The Treasury and the Comptroller General issue funds from the Exchequer Account to the Paymaster General for the departments, according to grants of Parliament for the Votes.

The departments spend the money through the Paymaster General.

On March 31st the Exchequer Account is closed and a balance is struck of issues and receipts.

After an interval to allow outstanding orders to

be paid, Accounting Officers prepare Appropriation Accounts, showing how the money granted for each Vote has been spent.

The Appropriation Accounts are audited by the Auditor General, who reports upon them to the Public Accounts Committee of the House of Commons.

The Public Accounts Committee reports on the Appropriation Accounts to the House of Commons.

Thus the financial business of the year and the accounts thereof begin and end in Parliament; and through the Treasury, Comptroller General, Accounting Officers, Auditor General, and Public Accounts Committee, the circle of Parliamentary control is completed.

# DEBT

# CHAPTER IX

## THE NATIONAL DEBT

### 1. General; and Funded Debt

Before we examine in detail the different forms in which our National Debt is held, let us stand aside and consider briefly the reasons why the British Government has to borrow.

There are times in the history of every nation at which it has to make a special effort. A war has to be fought, a natural catastrophe has to be made good, or a great reform in the social order has to be carried out. Special efforts of the sort cost money. They cost so much that it would be impossible to raise enough for them by means of taxation while they are being made. To pay for them money must be borrowed, and in order to borrow it the borrowing nation must be prepared with some asset to pledge to the lender as security for what he lends. What a nation has to pledge is its permanent taxable capacity. By pledging that to a borrower for a loan on the spot, it distributes the burden of the cost of its special effort over the generations. Posterity is called upon to help in paying for the special effort; and it is fair that it should be, because by the preservation of the existence of the nation against its enemies, by its reparation after a natural catastrophe, or by some great and permanent reform in its social

organisation, future generations benefit no less than the present.

We have had our share of these expensive times of special effort, and their legacy is our big national debt. War has been responsible for by far the greater part. Amongst natural catastrophes that have added to it was the Irish famine of 1848. Some £9,000,000 was borrowed then and added to the National Debt to keep the people of Ireland alive. Prominent amongst social reforms for which we are still paying is the abolition of slavery in 1836. In that and the following year £20,000,000 was borrowed and added to the National Debt to compensate the owners of slaves, and to rid us for all time of a stain upon our civilisation. The acquisition by the State of shares in the Suez Canal and of the telephone system could not have been financed from the revenue of the year.

In addition to these special efforts, minor fluctuations disturbing the balance of revenue and expenditure cause temporary increases and decreases of the indebtedness of the State. Some of these fluctuations are seasonal and can be predicted with a measure of accuracy; for example, a large proportion of the income-tax due in any year will not be paid until the last possible date; brewers, distillers, and importers of tobacco will not clear their stocks or pay their duties at times which the Treasury would find convenient. They have an awkward habit of postponing payment of as much of the duties as they can until the end of the year, in the hope of a reduction of the rate in the new budget; and then, if they think the duty will be reduced, of further postponing payment into the next year, or if they think that it will not be reduced, still more if they

think that it will be increased, of clearing their stocks and making big revenue payments in a lump and a hurry.

Some of these fluctuations, on the other hand, cannot be foreseen at all: to estimate in advance the revenue of a year is far from easy, but to forecast that of a particular week is impossible. But expenditure goes more or less steadily on; the salaries of the servants of the State cannot be postponed because A and B and C delay to pay their taxes, or a battleship be left half-built because rich men are unconscionably slow in dying and leaving their estates to enrich the Exchequer with death duties.

The period for which money must be borrowed will differ in all these cases; for a great war the State may have to raise loans which cannot be repaid for years or even generations; for a temporary shortage of revenue it may need accommodation only for a few days. As we should expect, the forms of borrowing vary just as the duration of the need varies. We will glance here at the different forms which Government borrowing in the United Kingdom has taken or may take, reserving to later pages a more detailed examination of their characteristics.

(1) First there is the Funded Debt, a term as much misused as it is familiar. Funded Debt strictly includes nothing but perpetual annuities, that is, stock the principal of which the Government need not repay until it wishes. Of such is the chief pre-war stock of the United Kingdom, Consols, which has been described as "the premier stock of the world." Only one of the war issues is funded—the

$3\frac{1}{2}$ per cent. Conversion Loan. The whole amount of this loan outstanding has been brought into existence by conversion operations of the sort to be described shortly: none has been offered for subscription in cash. The Conversion Loan and Consols with a remnant of the old $2\frac{3}{4}$ per cents., or "Childers," make up the bulk of the Funded Debt at the present time. The balance consists of the Government's permanent debt of £11,015,000 to the Bank of England (and a corresponding debt of £2,631,000 to the Bank of Ireland). This has been gradually accumulated as the result of a number of loans by the Bank to the Government at various times. On it the Government pays interest, and since the conversion of Consols to a $2\frac{1}{2}$ per cent. basis that has been the rate of interest paid. It has a special feature of interest, that it serves as part of the security on which the Bank's issue of paper currency is based. Those who argue that the Bank should keep a bigger reserve of gold with which to secure its notes sometimes suggest that a good way of enabling the Bank to get more gold would be for the Government to pay off its debt, and then the Bank could buy gold with the money. When that suggestion comes to the front the Government's debt to the Bank becomes interesting; but we must not allow that to draw us aside into questions of banking and currency which do not concern us.

(2) Next come those intermediate stocks which, though not funded in the strict sense, are yet not redeemable until a distant date or dates. Redeemable stocks were not issued in this country until the war, for the British public was content to hold an amount of Consols and other funded debt sufficient to cover the whole long-term indebtedness

of the State. It was not necessary to offer the additional inducement of redemption at a fixed date. These long-term loans shade imperceptibly into the longer issues of the pre-war "floating debt" or debt of early maturity.

(3) In the category of Floating Debt we may regard as a separate class Exchequer Bonds, and the similar National War Bonds and Treasury Bonds issued since 1914. Exchequer Bonds were recognised as part of the pre-war floating debt: their term might not exceed six years, but they were usually issued for three years and were held mainly by the Bank of England and the National Debt Commissioners. During the war the two other forms of Bonds just mentioned were created in addition, under limitations less strict than those governing the issue of Exchequer Bonds, and all three were issued to the public.

Exchequer Bills form a class by themselves, though they are now only of historical interest. They were invented by Charles Montagu, the celebrated Chancellor of the Exchequer under William III, about the year 1695, in order to supply the wants of the nation at the time of a great recoinage. They were current for a period of five years, but holders might claim repayment at par at the end of any complete year. But if interest rates had gone up during the currency of such a security, which had been issued at a fixed rate of interest, the capital value would correspondingly have gone down, and all holders would at the first opportunity have demanded repayment. Exchequer Bills were therefore not issued bearing a fixed rate of interest, but the rate was fixed every half-year at such a figure as would keep the Bills at par.

The most familiar and the most important part of the Floating Debt consists of Treasury Bills, which run usually for three months. These, with Advances, which are borrowings from day to day from the Bank of England or from such public departments as have balances to invest, will be described in detail in the chapter on Floating Debt.

It will be seen, then, that there is a wide choice of forms in which the British Government may ask Parliament for authority to borrow, each form suitable to a particular need. Why, for the great loans issued since 1914, which obviously could not be repaid for very many years, did not the British Government issue Consols or other funded stocks of a type familiar before the war? Let us first consider in more detail what Consols are, and then examine the reasons why the War Debt is represented, not by a single block of Consols, but by a bewildering mass of other Stocks, Bonds, Loans, and even Bills.

What are Consols? The answer to the question is simple, but is not as well known as it might be. Consols, of course, are a security for money paid, and the principal pre-war security of the British Government; but the exact nature of the security is often misunderstood. It can best be defined in the terms of the contract entered into by the British Government with one who buys Consols. The stock of Consols is divided into arbitrary amounts of pounds, shillings, and pence. A pennyworth of Consols is the smallest amount that any one can buy or hold. Let us notice that these units of pounds, shillings, and pence are simply convenient names for the subdivisions of the stock. There is

no necessary relation between £100 of stock and £100 in value. At the present time (April, 1924) I should pay only £57 for £100 of stock. Ten years ago it would have cost me £76; a few years earlier, as much as £112. This distinction is expressed by calling the £100 stock "£100 nominal." Now when I buy £100 nominal of stock, the Government makes a contract with me, and the contract which it makes is that it will pay me every year £2 10*s.* in quarterly instalments of 12*s.* 6*d.* on April, July, October, and January 5th. It reserves to itself the right to cancel the contract by paying me £100 if it chooses, that is, since 1923. What needs attention here is that the Government does not contract absolutely to repay the debt, represented by the £100 nominal of stock, at any given time. It may do so, since April 5th, 1923, if it likes; but only if it does like, and so long as the market value of £100 nominal of stock is less than the price of £100 at which it has, since that date, had the right to repay it, it will not like, for the simple reason that it would be cheaper for it to buy the stock at the market price than to repay it at £100.

All that my purchase of £100 nominal of stock gives me is the right to £2 10*s.* a year. It gives me no right to the repayment of £100 or of the money which I spent on the stock. What I have bought is, in fact, nothing other than a perpetual annuity of £2 10*s.*, subject to the Government's right to redeem it in the manner stated. Such is the nature of Consols and of Funded debt generally. Securities that must be repaid will gradually approximate in price as the day of repayment draws near to the price at which they will be repaid, as long as investors have confidence in the promise of repayment.

Lacking such a fixed price towards which to approximate, the price of £100 nominal of Consols varies with the varying rate of interest in the market for loans. The price of it is the price of a promise by the Government to pay to the holder £2 10*s*. a year, nothing more and nothing less. Now, when the supply of capital for investment is increasing in proportion to the demand for it, and borrowers are well supplied with funds to borrow, the rate of interest which they are willing to pay for loans falls: and when the supply is diminishing in proportion to the demand, and borrowers are ill supplied, that rate of interest rises. It follows that when the supply of capital for investment is increasing in proportion to the demand, the amount of it which must be given for a promise to pay a fixed amount of interest increases also. The price of Consols is the amount of capital to be given for a promise to pay a fixed rate of interest, so that price will rise and fall as the amount of capital for investment rises and falls, and as the market rate of interest for loans falls and rises. (It is, of course, now impossible for the price to rise appreciably *above* par.) One other circumstance only could interfere to upset the working of this rule, and that would be were investors to fear that the Government might not be able or willing to keep its promise to pay their fixed annual interest to holders of Consols. But as the credit of the British Government is the best in the world, that circumstance affects the price of Consols less, at any rate, than it affects the price of any other security; and so their price, better than that of any other security, measures the changes in the value of capital in the investment market.

We may now examine the reasons why issues of

huge blocks of Consols would have been unsuitable for the purposes of war finance. During a prolonged period of financial stress the rates which must be paid for the use of capital rise, as the capital available for investment becomes more scarce. This tendency is very much increased if for any reason the stock of legal tender money is being increased, so that the value of the currency depreciates in terms of goods and services; and such an increase is to a greater or less extent inevitable in a belligerent country. We have seen that an issue of Consols is the offer by the British Government of a fixed sterling income, paid quarterly for a long period or even, in theory, for ever, in exchange for a capital sum in the present. But if that capital sum in the present is monthly or even weekly becoming more sought after, and if also the quarterly return offered in exchange is likely for a long period to grow less and less adequate to purchase a given quantity of goods, it becomes necessary for a Government to offer the public some more certain future return. If, as generally happens, the return takes the form of repayment in cash, sometimes of slightly more than the amount borrowed, at a fixed date, the shorter the time which will elapse before repayment, the less will the investor require that the yield on his money shall represent an element of insurance against depreciation in addition to that of interest on capital. It may therefore happen that while the Government would prefer to issue as long-dated a security as possible, the investing public will demand one maturing at as early a date as can reasonably be asked. The history of the war loans is to some extent the tale of compromises between these opposing desires. We could not reconstruct in detail the

considerations affecting each war issue without reconstructing the hopes and fears of the Treasury, the Bank of England, the City, and the public at the time of each issue. One general tendency may be noticed in passing, which is that of all Governments to issue at par loans bearing a higher rate of interest, rather than loans at a lower rate, however familiar, at a discount: one of the reasons for this will appear later.

*Conversion.*—The terms upon which the Government borrowed during the war were to a large extent affected by the knowledge that money to borrow was decreasing in amount, and that the rate of interest to be paid for it was in consequence increasing. But now we have to contemplate the contrary state of affairs. It was always obvious that when the war was well over, the amount of money to borrow would increase, and rates of interest would fall again, though not for a long time to the pre-war level. That is, on the whole, what has happened. Rates of interest tend to fall, and the price of Government securities to rise. Paying the price in interest for its borrowings which had to be fixed during the dark days, the Government is paying more than it would have to pay were it to borrow now. It is therefore worth the while of the Government to make a fresh bargain with those who have lent to it, if by any means it can do so, in order to diminish the rate of interest which it has to pay.

Let us then consider how a fresh bargain having for its object a reduction in the rate of interest payable by the State, or some other advantage to the State, has been in the past, or may in the future be, effected. Such an operation is called a conversion.

It is impossible, without the most grievous harm to the credit of a State, to vary to the disadvantage of the individual investor any promise which was made to him and on the strength of which he lent the Government his money. This is a first principle which cannot be shirked or ignored. But what then can the Government do? Let us take the case of the 5 per cent. War Loan, rather than one of the old conversions by which other half-forgotten loans have been merged into Consols. It was provided in 1917 that the Government might repay the 5 per cent. War Loan at par at any time on or after the 1st June, 1929, on giving three months' notice in the London Gazette. That is, the Government can then compel every holder of this stock to accept £100 cash in redemption of each £100 nominal of his holding. It cannot *compel* him to accept anything else.

Now let us indulge in a little political optimism and assume that by June, 1929, Europe will be at peace, trade will be flourishing, capital abundant, and the rate for long-term loans steady at 3½ per cent. The Government may then offer to holders their choice between accepting £*x* of Consols or Conversion Loan or some other stock, *or* £100 cash for each £100 of their holding. Of the alternatives the former may be voluntarily accepted; only the latter can be made compulsory. If, for example, in the circumstances we are assuming, the offer was of £100 3½ per cent. Conversion Loan, many holders would no doubt accept it, but a proportion would be likely to prefer some other investment, and these would have to be paid off in cash. The amount of 5 per cent. War Loan outstanding on the 31st March, 1923, was over £2,000,000,000 and to find

a substantial portion of such an amount in cash would be impossible.

Conversion, then, is a new bargain, in which, as in an original issue, the Government must offer terms attractive enough to induce the majority of holders to accept its offer; it must be prepared to pay off the dissentients in cash, or to leave them for the moment in full possession of their original holdings. An offer of conversion cannot be effective unless the terms offered are more attractive to the holder than their present rights, in this case the right to ultimate repayment in cash.

The object of a conversion scheme may be the postponement of a maturing liability, without any decrease in the rate of interest. An example of such a conversion is the replacement of 5 per cent. National War Bonds by 5 per cent. War Loan; though this option was offered when the original issues of National War Bonds were made. Another object of a conversion scheme may be the substitution of internal for external debt: the three-year Notes and ten-year Bonds which we issued in the U.S.A. during the war are convertible into National War Bonds, and £21,000,000 were so converted in 1922–23. But whatever its object it has this essential characteristic, that it cannot compel holders to resign their legal rights. It must make them an offer which is attractive enough to persuade them to do so.

Lastly, in this survey of Government debt in general, let us consider the formal processes by which a Government loan comes into existence. The following account is of the practice before the war, which will no doubt become normal again in time. Variations

from this normal practice will be referred to in the next chapter.

When the Government wants to borrow money and to add the amount of the loan to the National Debt a resolution authorising the Treasury to make the issue is introduced to the House of Commons in the Committee of Ways and Means. When the loan is required to meet the excess of expenditure on Supply Services over revenue for the year, the form of the resolution is that "any money required for raising the supply granted to His Majesty for the service of the year may be raised up to an amount not exceeding £—— by means of an issue" of Consolidated 2½ per cent. stock, it may be, or of whatever other security the Government decides to issue. Statutory authority is given to the resolution by the next Consolidated Fund Act or Appropriation Act, or by a special Act. But without waiting for the final Act of the legislature, which takes time to get passed, the Treasury has authority to issue the stock as soon as the resolution has been passed in Committee. It is well that it should be so, because to have an issue of the sort hanging over its head upsets the whole financial community, and other would-be borrowers in particular. Besides, knowing that the issue had to come, some might be interested by operations on the Stock Exchange to raise the price of the stock, and so to make the issue more expensive to the Government. It is essential, however, that statutory authority for the issue should be obtained before the first payment of interest is made upon the new stock. To create the stock the simple process is that the Treasury issues a warrant for its creation to the Bank of England, and the Bank brings it into being by an entry on its registers. In

consultation with the Bank and its advisers on the Stock Exchange the Treasury fixes the price at which the issue is to be made. It fixes, that is, the price at which it will sell £100 nominal of the stock, carrying the right to receive, if the issue is of Consols, £2 10*s*. a year. The price is fixed by reference to the market price of Consols at the time. It is probably arranged that it shall be a trifle less than that market price, so as to make the offer look tempting to investors. A prospectus is issued announcing the offer to the public and inviting subscriptions. Lists of applicants are made out at the Bank of England; and if, as is often the case, more is applied for than is offered the amount offered is allotted amongst the subscribers in proportion to the amount which they asked for. When they have paid to the Bank the instalments of the purchase price the transaction is over; the national debt has had another permanent increase, and a fresh burden has been laid upon the shoulders of tax-paying posterity. All sums received in respect of an issue of Government stock are credited to the Exchequer Account, and out of that account they are drawn, as Exchequer issues, under statutory authority, to be spent upon the purposes for which they were raised.

Until 1911 Government securities were normally either inscribed in the books of the Bank of England ("inscribed stock" or "book stock") or were in bearer form ("stock certificates"). Holders of the former receive no negotiable document, but, just as any one with a banking account has a credit balance in the ledgers of his bank, so each stockholder has a credit balance of the stock which he holds in the ledgers at the Bank of England; and this stock

account is his holding and his title. To sell or transfer stock, he must either attend in person at the Bank, accompanied by some person (usually his stockbroker) who is personally known to the Bank, to identify him, and must sign away to the purchaser a part or the whole of his balance; or he must authorise a representative of his broker or his banker to act as his attorney and sign in the transfer books on his behalf. When this signature has been duly made in the transfer books, his stock account is debited with the amount transferred, just as his current account at a bank is debited when he cashes a cheque, and that of the new holder is similarly credited.

Stock certificates and bearer bonds are not surrounded with any formalities or precautions: they are, as their name implies, bearer documents, which must be kept with as much care as bank-notes; for while a holder cannot lose or destroy his holding of inscribed stock, possession of a stock certificate is his only title, which cannot be replaced if it is lost or stolen.

In 1911 a third form of holding was introduced, "registered stock" or "deed stock." This is registered in the books of the Bank, as is "book" stock, but in addition a certificate of registration is issued to the stockholder. Sale or transfer is by the "common form" of transfer deed, together with the surrender of the register certificate. A holder of deed stock who wishes to sell need neither attend at the Bank nor employ an attorney to attend there; and this form of holding is becoming very popular, especially in the provinces and Scotland, and among those who do not employ a London stockbroker for their investments.

Interest on inscribed and registered stock is paid

direct to the stockholders or their nominees by the Bank of England. The money for it is issued under the authority of the permanent Acts of Parliament which authorised the raising of the loans in respect of which it is paid, and it forms the chief part of the Consolidated Fund Services. Before each dividend date the Treasury sends to the Bank an authority to pay interest to the holders, which the Bank subsequently transmits to the Comptroller and Auditor General. Issues of funds for the payment of dividends are made as required from the Exchequer Account by the Treasury into a Dividend Account, on which the Bank draws to pay the stockholders.

There is always a certain number of holders who from indifference to lucre or ignorance leave their dividends unclaimed. Every year the Bank pays over to the National Debt Commissioners sums which have stood on its books as unclaimed dividends for five years and the Commissioners buy stock with these sums and put it to a separate account. When dividends have thus remained unclaimed for ten years the stock itself is transferred to the Commissioners also. But unclaimed stock and dividends can at any time be recovered from them by anybody who can make good his title. In some other countries this is not so, but the title lapses after a period of as little, in some cases, as five years.

# CHAPTER X

## THE NATIONAL DEBT

### 2. Long-Term Debt

We have seen that before the war the debt of the United Kingdom was all funded or floating debt, of which the latter was confined to borrowings for temporary requirements; and we have considered the process of conversion, by the operation of which this desirable state of affairs may again be reached. But this will not be for many years—perhaps not for a generation or two; and we must take stock of the large mass of debt which is neither funded nor floating. This is not the place for a history of British war finance, and we must content ourselves with noticing the principal innovations which appeared during the war period.

But first we may take, as illustrative of this intermediate class of debt, the one form of it which was in use in this country before the war, Exchequer Bonds.[1] We have seen that there are occasions on which the State is suddenly called upon to meet some item of expenditure too large to be financed out of the revenue of the year, but not large enough to justify a permanent addition to the fixed debt of the country. For such a purpose Exchequer

[1] Exchequer Bonds were classified as floating debt, but they fall more properly into the intermediate class now being considered, which did not then exist.

Bonds were the normal means of raising money. A case in point was the purchase by the State of the business of the National Telephone Company. Several millions had to be found as the purchase price. To have found them at once out of revenue would have meant extra taxation, and that would have given the taxpayer good cause to grumble. On the other hand, a business such as that of the Telephones should be made to pay for itself in time; its capital value should not be added to the dead-weight debt of the country. So to provide the greater part of the funds needed for its purchase an issue of Exchequer Bonds was created, and was handed over to the Company in part payment of the Government's debt. The Company sold the issue to its bankers at a price, and the bankers sold it to the public.

But when such an issue is made, arrangements ought to be made at the time for paying off the Bonds by degrees. Unless the Government makes an arrangement of the sort the whole amount falls due in a lump, and when that lump falls due the Government is probably no more able to find out of revenue the money to repay it than it was when the Bonds were first issued. Contrary to its original intention, it has to renew the securities or to convert them into fixed debt, both evil courses. Clear common sense as it is that Exchequer Bonds and any other sort of short-term issue should be arranged to fall due in sequence and not all together, the precaution has usually been neglected. To meet the cost of the South African War, for instance, £14,000,000 of Exchequer Bonds were issued (*inter alia*) in 1903, expiring all together in 1905. In 1905 of course there was not money enough in the

Exchequer to repay them all, and £10,000,000 had to be replaced by fresh Bonds. But this time it was provided that the new Bonds should be repaid by ten equal annual drawings of £1,000,000, with the result that in the course of the ten years the whole was safely paid off.

Another state of affairs in which an issue of Exchequer Bonds or other short-term security may be found convenient is that in which the Government wants to raise a loan for a purpose for which it does not object to add to its fixed debt, and cannot wait for the money; but, owing to the congested state of the market for loans at the time and the high rate of interest which it will have to pay, it thinks that it can do better by postponing for a time its final bargain with the lenders, borrowing temporarily in the meantime. It may then make an issue of a short-term security, repayable in a few years, and trust to finding a more favourable state of affairs in the money market at the future date when the security falls due, so that it may then convert the security into fixed debt on better terms than it could obtain in the present.

Operations of the sort are almost always bad finance. They amount to a gamble on the state of the loan market, and as often as not when the time for conversion comes the speculative Government finds that things have gone from bad to worse, and that it would have done better to have faced the music at once. There is a peculiar vice in the operation; it serves to delude the Government into supposing that it can escape from the restraint put upon it by the opinion which lenders have of its credit. A Government that refuses to temporise

to the wholesome control of the public opinion of investors. If investors dislike the purpose for which it proposes to borrow, or the idea of its making any increase in its debt at all, they refuse to lend to it except at a prohibitive rate. The Government must then postpone its borrowing or give it up altogether, and that is what it ought to do, because there is no judge of the expediency and prudence of a loan so good as an investor who is asked to find money for it. But if, when the investor shakes his head over a proposed loan and asks for a prohibitive rate, the Government says, "Very well; take your usury on a short-term security to be repaid in a year or two. Then we will convert the floating debt into fixed debt, and perhaps something lucky may have turned up by that time, to make things easier for us," it is then dodging the restraint which public opinion is seeking to put upon its borrowings. Does it get much good out of the transaction? It gets its money, of course; but it would probably have been better without it. By exhibiting itself as forced to borrow for short periods at high rates it injures its credit. The hawking about of its short-term bonds and bills constantly advertises its difficulties; and when the time for their repayment comes, at which it once hoped to be able to convert them into fixed debt on favourable terms, it probably finds that the operation which was intended to tide over its evil days has had no other effect than to prolong them. The short-term securities have then to be renewed at still more exorbitant rates because of the fresh advertisement which their renewal gives to the difficulties of the borrower. Worse still, the gamble on the state of the money market involved in the short-term issue may turn

out so conspicuously ill that the Bonds fall due at a time of panic amongst lenders, when a loan can hardly be obtained at any price. That is a risk inherent in the issue of any security which must be repaid without option on a given day; and it is a risk which should not be lightly run by responsible financiers. Another objection to this form of borrowing is that it is so fatally easy. In the early days of the vice, before a Government has become too notorious an issuer of short-term Bonds and Notes, and while its credit is still good, it can always find a ready market for securities of the sort with big banks and financiers. It has only to drop a bond into the bank, and the money runs out without trouble and without all the publicity and uncertainty of an offer to the public and to the small investor. It is as easy as the first steps of another descent, and by its ease it tempts the Government into reckless borrowings for purposes which are not absolutely essential.

However, the British Government is at normal times almost free from the special temptations which attend the practice of borrowing for general purposes on short-term securities. With the highest credit in the world, it is always able to borrow, in normal times, by means of permanent and fixed loans on reasonable terms. It is therefore at very exceptional times only that it is legitimate for it to borrow by means of short-term securities with the intention of converting them into fixed debt on maturity. At times such as war times it may have an urgent need to borrow which it cannot postpone, and owing to the troubled state of the world it may not be able to borrow the money permanently save at a very high rate of interest. It may then be

inevitable that it should borrow the money on short-term securities with a view to their conversion into permanent debt on more favourable terms when they fall due. But that can only be prudent if it is wholly impossible to postpone the borrowing; and it needs an emergency as great as that of war to oust the presumption that, if the rate of interest which investors ask is very high, it is because the borrower has no business to be borrowing at all.

The magnitude of the emergency of 1914–1918 is, however, not in dispute, and we may turn to the unusual features of the fixed-term loans then issued.

The first variation from the model issue described in the last chapter is that practically all the war issues after the first were without limit of amount. This needs no explanation.

We have seen (p. 209) that one of the reasons for offering to repay the capital sums borrowed, in some cases with a redemption premium in addition, at a fixed date was that borrowers required security against depreciation; and some of the innovations connected with these issues were additional ways of giving this security. For instance, some loans[1] were issued with a promise that they would be accepted at par plus accrued interest in payment for future long-dated war issues. Some, in the same way, would be accepted at the price of issue for the payment of death duties and certain other taxes.[2] Holders of these issues were thus assured both of ultimate repayment at par or better, and, in case they needed to realise them earlier, of the

[1] *E.g.* 4½ per cent. War Loan; 6 per cent. Exchequer Bonds; National War Bonds (Series I, II, & III).

[2] *E.g.* 5 per cent. War Loan; 5 per cent. Exchequer Bonds, 1922; National War Bonds (Series I, II, & III).

power to use them for certain purposes as equivalent to the original cash subscribed.

An extension of the principle of fixed repayment is found in one or two issues of Bonds [1] which, like Exchequer Bills (see p. 205), were made repayable in any year (or in certain years) of their currency at the option of the holder.

The same object was responsible for the issue of other War Loans with a depreciation fund provision. It will be simplest to consider a particular case. In the prospectus of the 5 per cent. War Loan we find an undertaking that when the market price of the stock falls below the issue price, the Government will set aside every month $\frac{1}{8}$ per cent. of the amount outstanding to be used in buying up the stock in the market. The result of this is of course to support the price of the stock. This is also one of the effects of a separate sinking fund earmarked to a particular stock; for example, the 4 per cent. Funding Loan has its own sinking fund, which works as follows: $2\frac{1}{4}$ per cent. of the original amount of the loan is set aside every six months. Out of this is paid the interest due for the half-year, and the balance is used to buy up stock below par, or, when the stock reaches par, to accumulate against the day of repayment. The $3\frac{1}{2}$ per cent. Conversion Loan has a similar provision. We shall find reason to doubt, when we come to consider sinking funds, whether such devices, which bolster up the prestige of one Government stock at the expense, it may be, of the others, are desirable.

Yet another plan for counteracting the fear of a rise in interest rates was made use of in connection with the 5–15 year Treasury Bonds 1925–35. These

[1] $5\frac{1}{2}$ per cent. Exchequer Bonds, 1925; 5–15 year Treasury Bonds.

bear interest at 5 per cent., *plus*, in each half-year, additional interest of 1 per cent. if the average Treasury Bill rate for the preceding half-year was between 5½ per cent. and 6½ per cent., or of 2 per cent. if that rate was 6½ per cent. or over.

One disadvantage of large fixed issues is that in practice money becomes available for investment not in large quantities at fixed dates, but at irregular times and in varying amounts. Some people may be so patriotic that they will allow large unremunerative balances to accumulate until the Government issues its next loan, but there must always be a large proportion who wish to invest their surpluses as they become available. If there is no Government loan on offer, they will buy in the market; this is good for the national credit generally, but gives no immediate help to a Government hungry for "new money." Accordingly, some issues of Bonds, notably the first (3 per cent. Exchequer Bonds 1920), and some of those issued after the war, were not offered at a fixed price but by tender, following the normal practice for Treasury Bills. The advantage of this is that the offer of such Bonds can be left open over a long period: rates of interest may fluctuate, but their fluctuations are automatically reflected in the price which the public offers, and much of the new money is gathered in as it becomes available for investment.

Other issues of Bonds were made "on tap," at a fixed price: when interest rates fell and the issue became too expensive to the Government, the tap was turned off until a new tap issue at a higher price could be put on the market.

Investors on a large scale, particularly Banks and Companies, put available funds temporarily

into Treasury Bills, and in order that they might be able to transfer into new loans without selling their Bills and competing for the moment with the Government for cash, Treasury Bills were accepted under discount for subscriptions to some of the larger loans (*e.g.* 5 per cent. War Loan).

Other special provisions may be classed together as inducements to special classes of investors. For the small investor the chief inducements were connected with the machinery of issue: practically all the War Loans could be bought on a relatively smaller scale through the Post Office Savings Bank, and held not on the books of the Bank of England, but on the Post Office Register, the arrangements for investment and sale being made as simple as possible. Similarly issues were also made through the Trustee Savings Banks. For investment on the smallest scale War Savings Certificates were introduced (see p. 246).

A concession of value both to the small investor and to many others was given in certain loans by allowing the dividends to be issued without deduction of income tax at the source. The normal practice is for the Bank of England to retain out of dividends of more than £5 which it pays for the Government the amount of income tax due on those dividends at the standard rate. It then pays the tax over in a lump to the Inland Revenue. But the smaller investor may not be liable to pay at the full standard rate, and if the full amount has been deducted, he has the trouble of making good a claim to repayment. Other classes of investors also prefer to have the use of the full dividend until the end of the financial year: and a third class again, who are taxed on the basis of the previous

year's income, may lose by deduction at the source a full year's use of the amount. To all of these the 5 per cent. War Loan and some others were made more attractive by the provision that dividends should be paid in full.

An enlargement of this concession was given to banks by a provision that dividends on their original subscriptions to any loan issued for the purposes of the war might similarly be paid in full.

A much larger income-tax inducement was the issue of certain loans of which the income was exempt from income tax. These were issued in double harness with taxable loans. Thus the 5 per cent. War Loan and the 5 per cent. National War Bonds had tax-free 4 per cent. satellites. Some more recent issues have been free of Corporation Profits Tax.

Among these varied attractions to investors, the one inducement to the gambling spirit may be excused as being a very little one. There was an agitation during the war in favour of an issue of Premium or Lottery Bonds, which would no doubt have brought in some subscriptions which were never attracted by the issues that were made. The proposal was rejected, but in 1919 the excitement of victory led our staid financial rulers to cut one little caper. Victory Bonds were issued at 85, with a sinking fund like that of the Funding Loan (see above): but while the latter is used in buying up stock in the market, the $2\frac{1}{2}$ per cent. set aside for Victory Bonds is applied after payment of interest, to redemption of drawn bonds at par. So the investor whose bond is drawn early for redemption gets an addition of £15 within a few years to the £85 which he lent.

From 1915 to 1920 most loans were issued free from British taxation to holders abroad; but more recently the Government has been able to afford the policy of converting external into internal debt, and this provision has not appeared since 1920.

Besides offering this inducement to investors in foreign countries, the British Government also borrowed abroad for the purposes of the war. By far the largest of these borrowings, and the only one with which we need concern ourselves, was the enormous sum raised in the U.S.A. This falls into two classes, loans issued on the American market, and borrowings from the American Government: the latter of course did not begin until the U.S.A. entered the war. Our loans issued on the American market, the first of which was a joint issue of the British and French Governments, amounted at the 31st March, 1919, to over $650,000,000. In addition there were outstanding at the same date a temporary loan from the bankers employed by the British Government and some dollar loans from other foreign countries: and some of the great armament firms and others in the U.S.A., from whom the Government made large purchases in the earlier years of the war, accepted payment in short-term securities, such as "Rifle Notes," just as a merchant will normally accept a bill of exchange from his solvent debtor.

While the issue of the war was in doubt, the security of the British Government had, for loans issued on the American market, to be reinforced by the deposit of collateral: this was provided by collecting the American securities held in this country: some were purchased by the Treasury (but many of these were sold outright in the U.S.A.); others were

lent to the Treasury by their owners, who received an additional ½ per cent. interest from the Exchequer. All of the latter class have now been brought back and restored to their owners.

These market borrowings were however the smaller part of our debt in the U.S.A.; for the loans made by the United States Government after America entered the war amounted to no less than $4,277,000,000 between the 25th April, 1917, and the 25th June, 1919. $80,000,000 was repaid up to August, 1920: thereafter a separate funding agreement settled the repayment of $122,000,000, which was lent in silver for the currency needs of India. This left a total of $4,075,000,000.

All this amount, like the sterling advances which we made to the Colonies and Dominions, was in the form of floating debt, repayable at call. But repayment at call of such an amount was of course impossible, and in 1923 the Chancellor of the Exchequer and the Governor of the Bank of England visited the United States to discuss the terms of repayment. The result is the Funding Agreement of June, 1923 (Cd. 1912 of 1923), under which the $4,075,000,000, with accrued interest bringing the total to $4,600,000,000, is now being repaid with interest at 3 per cent. for the first ten years and 3½ per cent. thereafter over a period of 61 years.

## Terminable Annuities

The Funding Agreement has not converted our debt to the U.S.A. into "funded debt," but into a Terminable Annuity: and the debts owed to us by some of the Dominions, which were also originally in the form of short term advances, have now been

converted into this form of debt, which on a smaller scale has been part of our regular financial system for many years.

Of Terminable Annuities the sort best known to the unfinancial man is the life annuity which is bought by an aged person with a small capital and nobody to whom to leave it when he dies. He pays his capital over to an insurance office which undertakes to pay him in return so much a year until his death, on condition that it shall then have for its own all that is left of his payment. On this understanding it will pay him more every year than he could get by investing his capital at interest. The essential characteristic of the arrangement is that his capital is returned in instalments to the holder of the annuity; and that is the essential characteristic of every Terminable Annuity. It is a contract by which a lender, the annuitant, advances a sum to a borrower, and receives in return a limited number of periodic payments, calculated to return to him bit by bit the sum advanced, together with interest on the amount outstanding at the time of each payment. Thus each periodic payment is made up of something for interest and something for capital. A life annuitant probably spends the whole as income. Under other circumstances, when one receives an annuity in return for an advance, the part due to capital repaid may be invested in some other security, and then when the last periodic payment of the annuity has been made, there is the whole capital amount of the advance, safely replaced and intact, and the annuitant has received interest on it in the meantime.

When the Government wants to raise a small capital sum and to arrange for its gradual repayment

out of revenue over a term of years, no way of doing so is as convenient as the creation and sale of a Terminable Annuity. Statutory authority is needed for its creation, as for that of any other form of debt. When that has been obtained, all that is necessary to create the annuity is an entry in the books of the Bank of England or of the National Debt Commissioners. When the Government has disposed of it to some annuitant, his name is entered on the register, the capital sum received from him is paid into the Exchequer Account, and the annual sum to be received by him for principal and interest is added to the general charge of the Consolidated Fund as a Consolidated Fund Service, or it is charged to the account of some particular Vote for a Supply Service. When all the instalments of the annuity have been paid the debt is wiped off and the annuity cancelled.

Money has been raised in this way at various times for several forms of capital expenditure, such as Naval and Military Works, grants or loans to Light Railway Companies, Public Buildings, and the acquisition of shares in the Anglo-Persian Oil Company. More important than any of these is the annual programme of telegraph and telephone construction, including occasionally the laying of a submarine cable, which is financed regularly by setting up annuities charged on the Post Office Vote. Authority for the borrowing is derived in each case from a special Act of Parliament which limits the total amount which may be borrowed, the rate of interest to be paid and the period for which the annuity may run. These annuities are not offered as investments to the public. There are some Government departments which always have

money to invest. Of these the Post Office itself, with big accumulations of capital through its savings bank, is the largest investor. Through the National Debt Commissioners, of whom more hereafter, they buy the Terminable Annuities as they are created. To them, through the same Commissioners, are paid the periodic instalments of the annuities, and as they are received the Commissioners re-invest that part of the instalments which represents capital, either in fresh annuities or in Government stocks. So part of the savings bank deposits received by the Post Office dodge round through the channel of an annuity charged upon the Votes back into use in the business of the Post Office. Sums received into the Exchequer Account in respect of these annuities are entered in the record of the Account in the Annual Finance Accounts as "Money raised by the Creation of Additional Debt"; and their expenditure is recorded by a corresponding entry of "Issues to meet capital expenditure." In making up the annual statement of the nation's total debt, its capital liability in respect of these annuities is calculated as the amount of capital included in the instalments which have still to be paid.

Instalments of the Terminable Annuities which we have just been considering are paid out of the appropriate Votes of Supply granted annually by Parliament, and the Government receives cash for them from the investors therein, of whom the chief are the National Debt Commissioners, as administrators of the funds which public departments have for investment. It spends the cash on its telegraphs and so on. Those circumstances distinguish them from another sort of annuity which

appears on the Finance Accounts as part of the debt of the nation. That other sort includes two annuities, one called the Savings Bank Annuity and one the Book Debt Annuity. They are a means of paying off not new borrowings but old debt and it will be more convenient to deal with them at the same time as Sinking Funds.

First in order of magnitude amongst Terminable Annuities as a capital liability, and last in order of importance as part of the financial machinery of Government, stands the nation's liability to the public in respect of annuities for life and terms of years. It is the result of the sale to private persons as investments of annuities of the commercial sort which has already been mentioned. Anybody can turn into the Office of the National Debt Commissioners in Old Jewry and buy from the Government an annuity for a term of years, for his life, or for two specified lives, paying for it a price which depends upon his age and the price of Consols at the moment. A long line of statutes beginning in the time of King George IV gives the Commissioners power to carry on this traffic, which is, in fact, a business undertaking in which they compete with the Life Assurance companies. Purchasers of these commodities may pay for them in money or Government stock; and if in money, then the Commissioners buy stock therewith; and the stock bought or transferred in respect of such annuities is cancelled. Instalments of the annuities are charged upon the Consolidated Fund. In the case of such commercial annuities, as in the case of the Terminable Annuities chargeable to Votes, the capital liability of the nation in respect of them is estimated as the amount of capital (as distinguished from interest) included in the remaining

instalments of the annuities. For annuities for terms of years the number of remaining instalments is certain; for life annuities it must be estimated with the help of tables showing the probable duration of human existence.

## CHAPTER XI

### FLOATING DEBT—SAVINGS CERTIFICATES AND CURRENCY NOTES

FLOATING Debt, as opposed to Funded Debt, strictly means all debt which is not in the form of perpetual annuities (with or without an option to the Government to repay the capital sum after a given date). But on the much larger scale on which the National Debt is now measured, the intermediate class of long-term debt referred to in the last chapter has come to be excluded from the common use of the term.

No hard-and-fast line can be drawn between floating debt and long-term debt, since any fixed term debt, whatever its original term, approximates more and more closely to floating debt as it nears maturity. A rough distinction may be drawn between Government short-term obligations which are held principally by the money market, and those which are mainly in the hands of the private investor; but the information necessary in order to distinguish in practice on these lines is not accessible to the public. In this chapter, therefore, general references to floating debt will include any such fixed term issues as are within a short time of their maturity, and which may be presumed, especially where the amount outstanding represents holdings in respect of which an offer of conversion has been made and not accepted,

to be likely to be presented for repayment in cash on maturity. When trade is stagnant and other more profitable investments are far to seek, it can confidently be expected that the bulk of such holdings, when repaid, will be re-invested in other, probably short-term Government securities, such as Treasury Bills or Bonds, but the proportion so re-lent to the Government will shrink in proportion to the increase of other openings for profitable investment.

A certain amount of Floating Debt is a regular and necessary part of the machinery of National Finance. In excess of that amount we have now (1924), and are likely to have for some time, an enormous amount of Floating Debt, which is a melancholy legacy of the war, and, far from being necessary is most undesirable. We will consider first the less unpleasing aspect of the subject, which is Floating Debt as a necessary part of the machinery.

We have noticed above (p. 202) that the inflow of revenue to the Exchequer fluctuates very considerably; and the effect of this fluctuation, so far as it cannot be counterbalanced by postponement or regulation of Exchequer issues for expenditure, must be that the Exchequer balance is at one time insufficient, at another excessive, for meeting the necessary outflow. We have now to consider the position which arises in normal times when revenue is temporarily insufficient to meet immediate expenditure. The machinery of borrowing in these circumstances has been little altered since before the war, though the scale on which borrowing is necessary is of course much greater now.

When an ordinary mortal finds himself with heavy expenses to meet, and no money with which to meet them, but with money enough coming in later on,

if he is foolish or quite without credit he goes to a money-lender; and if he is wise, and has some credit, he goes to his bank. His bank lends him as an overdraft the money which he needs, on the understanding that it is to be repaid out of his future receipts. Being wise, and having excellent credit, the Treasury too goes to its bank. When towards the beginning of the year and at dividend dates it finds that it will have to make issues out of the Exchequer faster than the revenue is coming in, in those lean months for revenue, it goes to the Bank of England and gets from it an advance, which is really an overdraft.

### Deficiency Advances

Before the war the chief item in the Consolidated Fund Services was the quarterly dividend on Consols, payable on the fifth day of each quarter. These dividends were included in the "account of the income and charge of the Consolidated Fund" for the preceding quarter under statutory authority, and the Treasury had permanent authority under the Exchequer and Audit Departments Act, 1866 (§ 12) to borrow from the Bank of England to meet any deficiency of income, as certified by the Comptroller and Auditor General on the "charge" so made up. Such advances were shown in the weekly Exchequer Account as "Temporary Advances, Advances by the Bank of England on account of the deficiency of the Consolidated Fund," and were known for short as "Deficiency Advances."

But the quarterly dividend on Consols is a bagatelle by post-war standards, and there are a dozen other influences, not necessarily at the beginning of the quarter, any one of which is more likely to affect

the sufficiency of the income of the Consolidated Fund than they: so this provision has fallen into disuse. In its place is the power given to the Treasury by the War Loan Acts to borrow on Ways and Means, *inter alia*, to meet maturing debt; and of this we shall hear more below.

### Ways and Means Advances

Since the revenue will not come in when it is wanted, the Treasury needs power also to borrow temporarily for Supply Services, and this power is given each year in the Consolidated Fund and Appropriation Acts. All such Acts, after authorising the Treasury to issue out of the Exchequer for the service of the year the lump sum granted by Parliament as Ways and Means, continue as follows:—

> "The Treasury may borrow from any person, by the issue of Treasury Bills or otherwise, and the Bank of England (and the Bank of Ireland) may advance to the Treasury on the credit of the said sum, any sum or sums not exceeding in the whole [the amount which the Act authorises the Treasury to issue]."

We leave the matter of Treasury Bills on one side for the present; it is the "otherwise" with which we are first concerned. In practice, "otherwise" consists in part of borrowing from the Bank of England on overdraft, in the same way as that in which Deficiency Advances are borrowed. If the Chancellor of the Exchequer finds at any time that the revenue is coming in so slowly in comparison with the issues which he has to make for Supply Services that it looks as if the balance on the Exchequer Account would be run inconveniently low, he writes to the Governor of the Bank of England

and asks him to have the goodness to consent to an advance during the current quarter of an amount not exceeding ——, and he mentions the amount. He also mentions the rate of interest which he proposes that the advance should bear (it must not be more than 5 per cent.), fixing it with reference to the Bank's official rate of discount. When the Bank has considered the matter, the Governor answers and tells the Chancellor that it has agreed to make the advance. So the advance is made and placed to the credit of the Exchequer Account. According to the terms of the Appropriation Act, principal and interest have to be repaid out of the revenue received into the account before the end of the quarter following that in which the advance was made. Advances of this sort, since they are borrowed on the credit of funds voted by Parliament for Ways and Means, to distinguish them from Deficiency Advances are called Ways and Means Advances, and appear in the weekly return of the Exchequer Account as "Temporary Advances, Advances by the Bank of England. On the credit of Ways and Means, by Other Advances—so much." In the ordinary course of things they are seldom necessary save at the end of a quarter, the time at which the departments are paying their bills, and, as we have seen, big issues are being made from the Exchequer Account for Supply Services to bring the accounts of the Votes and the balances in the hands of the Paymaster General into agreement with the grants of Parliament. We usually find therefore Ways and Means Advances from the Bank appearing in the Exchequer Account shortly before the end of the quarter or, in present circumstances, at the time of the dividend on, or maturity of, one of the War

Loans; and the repayment of the advances soon afterwards.

Advances made to the Government are shown in the books of the Bank as advances made on Government Securities. This is what they are, since the security for the advance is the Government's statutory obligation to repay it. In the weekly return, therefore, of the Bank's assets and liabilities, the item "Government Securities" is increased by the amount of the advance made.

The section of the Act quoted says that the Treasury may borrow "from any person, by the issue of Treasury Bills or otherwise." With Treasury Bills we will deal presently; the remainder of the "otherwise" is what we are here concerned with. These other Ways and Means advances are made by Public Departments which hold large balances for investment, such as the National Debt Office, which has the responsibility for investing the money deposited in the Savings Banks. This money is withdrawable on demand, and it must therefore be in great part invested in the most liquid securities which can be found: and Ways and Means advances, which the Government are prepared to repay at any time, are more nearly akin to cash than any investment open to the public. The Paymaster General's Department is another which often has funds available, representing deposit balances held on behalf of various departments, to lend for a short time in this way, and the cash received for Currency Notes may also be so used.

We have already, in 1924, reached the stage at which advances from the Bank are, as they were before 1914, really temporary: but the Public Departments' advances have not yet been reduced

to the same extent, and a large amount of these is still being carried forward from year to year. To that extent they are part of the legacy of the war, and not a part of the regular financial machinery of normal times.

### Treasury Bills

Now we come to Treasury Bills. When a house of business of any sort finds itself in a fix for money, because for instance it has to meet payments before the money out of which its payments are to be made has come into its hands, it goes first in many cases to its bank for an overdraft. But if its bank has lent it as much as it is convenient for it to lend, or if the borrower thinks that he can get the money which he needs cheaper elsewhere, he may raise it by means of a bill of exchange. In substance a bill of exchange is a promise to repay a certain sum of money specified in the bill to whoever may be the holder of it on a certain future date. Having made out a promise of the sort, the would-be borrower takes it to some rich person, a banker it may be or a bill broker, who makes a business of that sort of thing, and sells it to him for what it will fetch. If the names which appear on the bill, of the people who have made themselves liable to pay it, are those of substantial folk with good credit, the price which the buyer will pay for the bill is the sum which those people promise to pay at its maturity, less interest at the current rate on the money paid for the bill until the time at which the bill matures and the money is repaid. A bill of the sort, with good names upon it and maturing in a reasonably short time such as three months, is the safest security

in the world and the most convenient, and for that reason it is the cheapest way in the world of raising money.

In its temporary borrowings, the Treasury has now learned to imitate the procedure of the business house, and to supplement its overdrafts by borrowing on the security of bills. To the late Walter Bagehot, then editor of the *Economist*, is due the credit of pointing out to the Government the advantages of thus adapting to its needs the methods of commerce. The credit of the British Government, as he said, is the best in the world; and the best name in the world on the best security in the world makes an ideally cheap and convenient way in which to borrow money. If, he argued, the Treasury wanted to borrow money for short periods at the lowest possible rates, it should learn from its mercantile rivals in the loan market; it should compete for loans with commercial borrowers on an equal footing, making use of all the refinements and economies which they have invented to facilitate their borrowings, and in particular of the bill. So the Treasury did. By the Treasury Bills Act in 1877 (40 Vict. c. 2) the Treasury was given power to issue bills for certain purposes, with which we will deal hereafter. It was not, however, until 1902, that the power to borrow on Treasury Bills for Ways and Means was included in the section of Appropriation Acts and Consolidated Fund Acts quoted above. In that year the exceptional expenditure on the South African War greatly exceeded the revenue, and the temporary borrowings which were required were so large that it was inconvenient to the Bank of England to supply out of its own resources alone all the money needed as Ways and Means Advances. So power to borrow on

Treasury Bills also in anticipation of the revenue was given to the Treasury in order to enable it to draw upon a wider area of supply for its loans. It is now always provided in Annual Appropriation and Consolidated Fund Acts, in addition to the general authority already quoted, that the date of repayment of any Treasury Bills issued thereunder shall be a date not later than the end of the financial year in which the bills are issued and that a section of the Treasury Bills Act, 1877, which gives power to the Treasury to renew bills as they mature, shall not apply to these bills; that is, that they are not to be renewable, but must always be paid off as soon as they fall due.

Such are the function and the characteristics of Treasury Bills as a necessary part of the regular financial machinery. Every year there is some borrowing on Ways and Means Treasury Bills, as there was before the war, for the temporary needs of the year. But most of the Treasury Bills outstanding [1] are a legacy of the war, and not part of the necessary machinery. They have either come into existence by direct descent from bills issued during the war, or they have been issued to provide for the repayment of other maturing debt. For this purpose the War Loan Acts give a general authority to re-borrow. So these bills remain outstanding over the turn of the year, from March 31st to April 1st.

It is this mass of Treasury Bills, the legacy of war, that is responsible for the great change in the amount and the character of our Floating Debt, in post-war as compared with pre-war days. The chief change is, that an amount which was manageable has

[1] At the present time (1924) about 95 per cent. on an average.

become unmanageable. It would be impossible for the Government, however great the need, to find within a reasonable period of time, the wherewithal to pay off the amount now outstanding. But all the hundreds of millions of Treasury Bills fall due every three months, and much of the amount borrowed on Ways and Means may be required by the lenders at short notice. In the event of a sudden crisis, the credit of the Government would to some extent be clogged by its too present liabilities, and repayment to holders of Treasury Bills who let them run off would absorb much of any sums which could be raised. The consequences for the moment would be much the same as if British credit was lower than it is, and the rate of interest which would have to be paid would be out of proportion to the value of capital. Another consequence would be that the quantity of legal tender money would have to be very largely increased in order to satisfy the increased needs of the holders who demand repayment. For these reasons reduction of the Floating Debt is a paramount necessity. It is, in fact, being slowly reduced, by the application of surpluses as they accrue, and from time to time by the sale of bonds, and funding generally. Any such decrease at the end of a financial year is permanent, except in so far as it may be necessary to raise money later on bills for the redemption of maturing war debt. To make sure that the decrease shall be regular and permanent must for some time to come be one of the chief objects of our financial policy.

It was found convenient before the war to have a small part of the National Debt represented permanently by Treasury Bills, which were carried over by successive renewals from year to year.

These Bills, which were issued to the amount of some £14,500,000 under the authority of various Acts, usually in the form of six months' bills, were in substance almost as much a part of the fixed debt as Consols. There can be no doubt that a much larger amount than £14, 500,000 could with advantage to the money market and to the City as a whole be allowed to continue in existence for many years, and it is probable that when, in the happy future, the reduction of the Floating Debt is bringing it near to manageable dimensions, it will be found desirable to fix afresh an amount of Treasury Bills to be kept running on from year to year, as a permanent part of the National Debt.

Under whatever Act any particular bills are issued, the manner of their birth, life, and death is the same. And first we will deal with the manner of their birth. When the Treasury has made up its mind to make an issue of bills, it sends a warrant for the issue to the Bank of England, and leaves it to the Bank to do the work. The warrant is countersigned by the Comptroller and Auditor General, whose duty it is to see that there is Parliamentary authority for the issue. A public notice is sent out inviting tenders for the bills; it states their amount, the day[1] on which payment must be made for them, and the day on which they will be repaid. The notice is inserted in the official *London Gazette*, which appears on Tuesdays and Fridays, and it is circulated to bankers and financial houses in the City and elsewhere, who may be expected to

[1] At present the day may be any day in the week for which the offer is made, at the option of the tenderer: repayment is, of course, on the corresponding day three months later.

tender. Technical regulations as to terms of tender are laid down by the Treasury, under the statutory authority of the Treasury Bills Act of 1877.[1] When the day for tendering comes, the banks, bill-discounting companies, bill brokers and others, who make a business of financial operations of the sort, send in their tenders to the Bank of England. Their offers are expressed as the price which they are willing to pay for the issue or for a part of it, and they calculate that price by deducting from the amount which they will receive in repayment on the maturity of the bills a certain percentage as interest on the money which they advance, during the currency of the bill. This percentage is called the rate of discount. Tenderers fix the rate of discount, which is the interest which they are willing to accept on the money that they lend to the Treasury, in accordance with the state of the market for loans at the time that the tender is made. If the supply of funds for loans for a short period is small at the time, they will ask for a high rate of interest, and *vice versa*. At the Bank the tenders are considered in the office of the Chief Cashier. Some discrimination, we may suppose, is made as to the financial standing of the tenderers, and then the best tenders are accepted in order until the whole issue is provided for. An announcement is made for the benefit of the public that tenders at the rate of, say, £98 17*s*. 6*d*. per cent. will receive 20 per cent. of the amount applied for and "above in full." A statement of the average rate of successful tenders is also made which might in this case be £99 per cent., and of the total amount applied for, which is usually largely in excess of the total amount offered.

[1] Cp. Treasury Minutes 24/11/1904 and 31/5/1889.

During the war, when Government requirements were practically unlimited, bills were put on the market at fixed prices without limit of amount. Now that the tender system has been resumed, a survival of this fixed price issue is to be found in the issue of "tap" bills. After each weekly tender a rate is fixed and published at which additional bills may be bought. This rate is of course somewhat lower than the rate at which the tender bills were allotted.

Amounts received for Treasury Bills at the Bank of England are set to the credit of the Exchequer Account. Conversely, when the bills mature, if the Treasury decides to pay them off, the amount due on the bills is issued from the Exchequer Account to the Bank of England, and the Bank pays the holders.

### Savings Certificates

An interesting new form of borrowing was introduced during the war, designed to reach the very small investor: War Savings Certificates—later National Savings Certificates—were issued at the price of 15*s*. 6*d*. for each £1 certificate, which is repayable at £1 after five years and continues to bear interest up to ten years. The yield is free of income tax throughout. The most noticeable feature of these Certificates is that the rate of interest increases progressively: the full yield is not earned unless the Certificate is held for at least five years. The price was raised to 16*s*. on April 1st, 1922. It is very clear from the results obtained that these Savings Certificates, which were well advertised by Voluntary Savings Committees through the country, had a wide appeal: approximately 253,000,000 were taken up by the end of the war.

It is not possible to compare exactly the cost of borrowing on Savings Certificates with that of other forms of borrowing, because an unknown proportion are presented for repayment in the earlier years of their currency and so earn a lower return; but the value to the State of encouraging habits of thrift in new directions would probably justify an effective rate slightly in excess of that paid for other loans. That they have so encouraged thrift may fairly be deduced from the fact that since the war, though the patriotic appeal has been less strong, a further 400,000,000 have been sold.[1]

Savings Certificates may be presented for repayment at any time, though on terms which we have seen are less favourable than those given on maturity. They therefore constitute a "call" liability of the British Government; but the confidence shown by a similar class of holders, Post Office Savings Bank depositors, in the early days of the war, makes it unlikely that even in a severe financial crisis this would prove to be a danger.

### Currency Notes

One of the first effects of the crisis of August, 1914, was a scarcity of legal tender money, and on August 6th the Currency and Bank Notes Act, 1914, was passed, empowering the Treasury to issue currency notes for one pound and ten shillings, as legal tender for the payment in the United Kingdom of any amount. This is not the place to discuss the general questions connected with the issue of notes by the State, but some of the effects of this innovation are very closely connected with our subject.

[1] To the end of August, 1923.

Currency Notes were at first issued as advances to bankers, but this was only a temporary phase. The notes now in circulation have all been paid for by the banks through which they were issued, and the Government has received between £250,000,000 and £300,000,000 (net) in exchange for the notes which are in circulation. On this vast sum it has to pay no interest, but it must of course be prepared to redeem the whole of the notes outstanding if it ceases to issue notes, and, in the meantime, to redeem any notes which become surplus to the currency requirements of the country.[1] The problem is in many ways similar to that of providing for the repayment of Savings Bank deposits, and it has been dealt with in much the same way by setting up a Reserve Fund. This takes the form of an account at the Bank of England, called the Currency Note Redemption Account. Into this account are paid all the receipts when notes are being drawn out: from it the value of notes presented for cancellation is paid out to the holders.

Every day the Bank of England informs the Treasury of the net movement of the circulation and the amount which is consequently due to be received into or paid out from the account; and every week the Treasury publishes an Issue Account, giving the movement since the preceding week and the total of issues and cancellations of notes from the beginning, and also a balance-sheet of the account. From this balance-sheet we can see in what form the assets are held. We find that on December 13th, 1923, the balance on the account was £123,321, the gold held £27,000,000 and the Bank of England

[1] This may serve as an excuse for including Currency Notes in a chapter on Floating Debt.

notes £22,450,000, a total of £49,573,321 against liabilities to the holders of notes and certificates[1] of £288,679,316.

The next item in the assets is "Silver coin £7,000,000" and we may at first sight be inclined to regard this as cash in almost the same way as the preceding items. But strictly this is not so: it is true that silver is legal tender up to £2, but "the holder of a Currency Note shall be entitled to obtain on demand, during office hours at the Bank of England, payment for the note at its face value in *gold* coin" (Act of 1914). In present circumstances this is no great matter: we know that during and since the war gold has been worth more than its statutory value and that we cannot in practice insist on payment in gold at the moment.[2] We should therefore expect that this holding of silver is not a permanent part of the reserve fund against the Currency Note issue, but that it is finding a temporary resting place there during the process of replacing the old silver coin of the country by that coined since 1920. The rest of the assets are Government Securities: we may reasonably conjecture that short-dated securities such as Treasury Bills form a considerable part of this item.

But there is still one item in the balance-sheet which we have not mentioned: this appears on the liabilities side as "Investments Reserve Account £12,075,370," and it is balanced by a corresponding

[1] Currency Note Certificates are not allowed into circulation: they are merely a means of economising paper and printing and storage room; each is for £100,000 and they are earmarked at the Bank of England for the note-issuing banks which may hold Currency Notes against their issue.

[2] The two chief purposes for which sovereigns might now be needed are for melting or for export: and both are at the present time illegal.

amount included in Government Securities. For an explanation of this we must turn to a Treasury Minute of May 3rd, 1915 (Cd. 7918), where we find it laid down that the interest earned by the account on its Government Securities is to be applied in the first place to form a fund to meet any losses which may be incurred on the realisation of those securities. This is in fact an ordinary reserve fund against depreciation of investments, the amount of which is fixed by the Treasury; it stands at present at 5 per cent. of the total securities held. The main tendency in the last two or three years has been for Government securities to appreciate, and it is not likely that this percentage will need to be increased unless the national credit is adversely affected by some such misfortune as another war.

After providing for this reserve, the balance of the interest earned is paid into the Exchequer, the amount being shown each year in the Finance Accounts; in 1922-23 it was £13,340,000.

The amount of the note issue raises questions too large for discussion here. Suffice it to say that at present the limit placed on the fiduciary issue, that is the notes not backed by gold or Bank of England notes, is that recommended by the Committee on Currency and Foreign Exchanges after the war. The fiduciary issue in any year may not exceed the maximum actual fiduciary issue of the preceding year.[1] As long as this restriction is maintained, the fiduciary circulation must decrease, or at any rate cannot increase.

[1] Treasury Minute of the 15th December, 1919 (Cmd. 485 of 1919).

# CHAPTER XII

## CONTINGENT LIABILITIES—THE NATIONAL DEBT OFFICE: ASSETS

THERE are some big debts for which the Government has a liability which is contingent only; it promises to pay them if somebody else does not. For the most part the Government does get some return in cash out of the objects for which these debts were incurred, and so they are not "dead-weight" debt. There is a large number of contingent or guaranteed loans of the sort. With most of them we need not trouble ourselves, because they are exceptional affairs which do not form part of the regular structure of our finances. Such are the loans to Greece, Turkey, and Egypt, which we have guaranteed at one time or another for political reasons, in order to help those permanently impecunious countries to raise the much-needed wind. Nor need we trouble about the similar guarantees given to the Transvaal (after the Boer War), the Sudan (for a big irrigation scheme), and Mauritius; and more recently Northern Ireland. All these are exceptional and temporary. But there are some guaranteed loans raised for our own social purposes to which we must give some attention. They are the Local Loans, and Irish Land Stock, and a series of issues for private bodies which the Government has guaranteed under the provisions of the Trade Facilities and Export Credit Acts.

### Local Loans

Let us deal first with the oldest institution, Local Loans. Local authorities have of course their own revenues from the rates; but at times they need in addition capital in lump sums in order to discharge their duties under many Acts of Parliament, of which the chief are the Education, the Poor Law, the Public Health, and Small Holdings Acts, and, latest and largest, Housing. They need it to spend, for example, on sewers, on the purchase of land for small holdings, and on other public purposes which are constantly increasing in number and in cost. It would be inconvenient that all these little public borrowers should be running about competing for money in the public loan market; they would have to pay high rates of interest, and they would be making bad bargains and getting into difficulties. So, when imposing upon them duties which make it necessary for them to have capital, Parliament has undertaken at the same time to provide them with the capital which they need. It does not provide it out of the annual revenue; the burden would be too heavy. It borrows the money and then re-lends it to the local authorities. For this purpose a capital fund has been established, called the Local Loans Fund. Money is raised for it by the issue to investors of stock called Local Loans Stock. This bears interest at 3 per cent., and it has been redeemable at par, if the Government should please, since 1912. Since its market value is much below par, that is a barren right. As the requirements of local authorities have increased fresh stock has been issued from time to time, and the total amount now outstanding is nearly £220,000,000. Sometimes the

stock has been issued publicly and sold to investors at large in return for their savings; sometimes it has been handed over privately to the National Debt Commissioners as an investment for the big sums which they are always receiving for investment from the Post Office and other public departments. The primary security for the stock is the assets of the Local Loans Fund; we shall see what those assets are. In addition the Government guarantees the interest on the stock should the primary security prove inadequate. It does not guarantee the principal of it, though, as we shall see, it does protect its assets.

The Local Loans Fund is an account to the credit of which is set in the first place the money received from investors for Local Loans Stock as it is issued from time to time.[1] It is managed by the National Debt Commissioners. Out of it is drawn the money advanced as loans to the local authorities to meet their needs for capital. Interest is received in return; and the interest received from the local authorities on the loans made to them, and the repayments which they have to make as instalments of the capital of those loans, are paid into the Fund. A separate account is kept of payments on account of interest and on account of capital. Out of the Fund the Commissioners draw the 3 per cent. interest which has to be paid to the holders of Local Loans Stock, and money with which to pay for the expenses of the management of the Fund.

[1] In 1888, in accordance with the provision of the Local Loans Act of 1887 by which the fund was founded as a preliminary to the Goschen conversion scheme, a first issue of 36·5 millions of stock was created and issued to the National Debt Commissioners as security for Local Loans in lieu of other forms of security therefor then outstanding. The total has been raised to the present figure by subsequent issues of stock.

Commonly interest received from the local authorities is greater than interest paid to holders of Local Loans Stock with expenses thrown in; so that the Fund is run at a profit. Annual profit is set to a Surplus Income Account, which is used to make good any loss of capital owing to the issue of Local Loans Stock at a discount. At times when there is no special activity to be financed, instalments repaid annually by local authorities in respect of the principal of the loans made to them are enough to provide the greater part of the capital needed to make fresh loans with. If there were no fresh loans to make they would be used to redeem Local Loans Stock, or they could be invested in other securities and so accumulated for the purpose of redeeming Local Loans Stock some day. But as a matter of fact there are always fresh loans to make, and by using for those loans the instalments of capital repaid the amount of fresh Local Loans Stock which has to be issued to investors is kept down. Keeping down the amount of such stock which has to be issued afresh is as useful work for the instalments as redeeming the outstanding stock. The effect is the same.

So the capital of the Fund is constantly being turned over, but in normal times nearly as much comes in during the year as goes out, and fresh issues of Local Loans Stock are only needed because of the new work requiring additional capital expenditure which is constantly being given by Parliament to the local authorities. One of the largest of these tasks that has ever been imposed is the recent Housing programme which has made large new issues necessary since the war.

The National Debt Commissioners do not themselves make the loans directly to the local authorities

or receive directly the payments of interest and principal from them. To do that a special body has been established, whose name is the Public Works Loans Commission, and whose local habitation is at the office of the National Debt Commissioners in Old Jewry. Acting under statutory authority it considers applications for loans from local authorities and others and arranges to make loans to them, receiving funds with which to make the loans from the National Debt Commissioners. Local authorities pay interest and annual instalments in repayment of the principal of their loans to the Public Works Loans Commissioners. As to the great bulk of the loans the Public Works Loans Commissioners' security for the loans to local authorities is local rates; as to a small part it is some special property of the local authority such as a dock, a harbour, or a pier. A bond is given by the local authority to the Public Works Loans Commissioners, which is the visible evidence of the security pledged to them. The Public Works Loans Commissioners in their turn pay over interest and annual instalments in repayment of principal to the National Debt Commissioners for the Local Loans Fund. The amount which may be advanced by the National Debt Commissioners to the Public Works Loans Commissioners in any year—and therefore also the amount which may be advanced by the latter to local authorities—is controlled by an annual Act of Parliament, the Public Works Loans Act, which specifies the total amount which the National Debt Commissioners may issue in the year for the purpose of local loans.

Directly the security for Local Loans Stock is the assets of the Local Loans Fund, of which the chief is the capital debt to that Fund of the Public

Works Loans Commissioners. To meet their liability to repay that debt the Public Works Loans Commissioners depend ultimately upon the rates due to the local authorities to whom they have made advances, and upon a little special property also; so that ultimately those are the true security for Local Loans Stock. The Government's guarantee of interest would become operative only if the rates, etc., should prove inadequate to maintain the assets of the Fund. Since the Fund has turned out to be self-supporting, the Exchequer has never been called upon for a contribution. Technically Parliament does not guarantee the capital of the stock. But if it is found that the capital of any loan cannot be recovered and has to be written off the assets of the Fund, Parliament has to make good the loss. It is enacted in the Local Loans Act of 1887 that that part of the principal of any of the loans which has turned out to be irrecoverable is to be written off from the assets of the Fund. This is done each year by the Public Works Loan Act; and in the next Civil Service Estimate a special grant is made for the repayment to the Fund out of the Exchequer of money enough to make good the sum written off. Thus Parliament does in fact protect the assets of the Fund and the security for the capital of Local Loans Stock from its chief source of loss. But it does not guarantee the holders of the stock from loss due to the depreciation of the market value of their stock caused by general circumstances such as the rise in the rate of interest on all loans.

Such is the machinery by which Parliament provides money for the capital expenditure on public works of the lesser local authorities. It is only for the lesser authorities that money is thus provided;

They alone need the help, because of their inferior credit. Big local authorities, such as the great cities and counties, do not need to have their credit backed by a Government guarantee in order to borrow money cheaply. London, Liverpool, or Birmingham can go into the open loan market and borrow on their own credit almost as cheaply as the British Government can. They do so; making public issues of their stock, or selling their bonds privately to banks and other investors. But those borrowings are made on their own credit alone. The British Government has no sort or kind of liability for them. If London failed to pay the interest on its stock it would be no concern of the taxpayers of the United Kingdom, but of the ratepayers of London only. Such municipal and local borrowings are no part of the structure of national finance. A contingent liability for the interest on Local Loans Stock is the only liability which the Exchequer and the taxpayer have in respect of local borrowings. They undertake it to give a helping hand to small local authorities which have expensive duties cast upon them by the taxpayers' representatives in Parliament, and are not rich enough to go and borrow publicly on their own credit alone.

Another use has been made of the machinery of the Local Loans Fund. Provision was made by the Colonial Loans Act of 1899 for charging on that Fund fixed loans to poor colonies and protectorates, which are not rich enough to borrow money cheaply on their own credit. In their case the process of advance and repayment is exactly the same as in the case of loans to local authorities, save that it is the Treasury and not the Public Works Loans Commissioners that makes the advance, and that the security

for the advance is the revenues of the colony. Several of the West Indian Islands, Seychelles, and Cyprus, have had advances of the sort, and the latest was an advance of £3,000,000 authorised in 1914 for the British East African Protectorates.

### Irish Land Stock

The second in size of the contingent liabilities of the Exchequer is in respect of Irish Land Stock. Crowning the long effort to buy out the Irish Landlords an Act was passed in 1903, when the late Mr. Wyndham was Chief Secretary for Ireland, to provide for the wholesale purchase of the land of Ireland from the landlords, and for its re-sale to the tenants. It was arranged that money for the purchase should be provided in the first place by the issue of a Government Stock to be called Guaranteed Irish Land Stock. This carried interest at 2¾ per cent. and was redeemable at the option of the Government in and after 1933. As the stock was issued the money received for it from investors was paid to a special fund, the Irish Land Purchase Fund, which is analogous to the Local Loans Fund. Later developments and modifications of the scheme, which included the issue of a 3 per cent. Stock, had by March 31st, 1923, brought the amount of stock in existence up to over £130,000,000, but the direct interest of the Exchequer in future purchases of land has been brought to an end in view of altered conditions in Ireland, and this existing liability will henceforward decrease steadily, though it will not be extinguished for half a century or more, i.e. till the Sinking Fund payments (which are added to the rent paid by the tenants) have

accumulated, at whatever rates may be obtainable, to the amount required to repay the stock.

## Export Credits

One of the consequences of the war was to impoverish many of the accustomed markets for British manufactures and consequently to make it necessary for exporters in this country to seek out new purchasers, and to build up new connections. The machinery by which export trade was mainly financed before the war was that of bills of exchange; these might be drawn by the exporter on his foreign client, accepted by the latter or his agent, and discounted in London; or, as was more usual, the bills might be drawn by the foreign importer on his representative (or an accepting house) in London and handed over to the exporter in payment for his goods.

With the opening of new channels of trade, often to countries first brought into existence by the Peace Treaties, there was naturally a lack of facilities, arising partly from uncertainty as to the financial stability of new customers and even Governments, and it was thought desirable for the Government to oil the wheels. Accordingly by the Overseas Trade (Credits and Insurance) Act, 1920, the Board of Trade was empowered, with the consent of the Treasury, and after consultation with an Advisory Committee set up under the Act, to grant credits to British traders and companies, or to undertake insurance, in respect of the export of British manufactures to the new European countries, within a limit of £26,000,000. Advances were made under this Act, at first not exceeding 80 per cent. of the cost of the goods exported, but later up to the whole cost, the exporter

remaining ultimately liable for any excess over 80 per cent. This part of the scheme was brought to an end at the end of 1922. The total amounts advanced to traders were £1,752,150, of which £346,704 had been repaid at the beginning of 1924.

The original Act was, however, amended in 1921 to cover the giving of guarantees; that is to say the Government might back the ordinary commercial bills by which export transactions are financed. The amending Act also extended the scheme to the British Empire. Later in the same year the scheme was further extended, power being given by the Trade Facilities Act, 1921, to give guarantees in respect of trade with any country.

The conditions under which guarantees are given are shortly as follows:—

(1) General Credits, over a period not exceeding 12 months. The applicant specifies the amount of the credit required and the country to which he intends to export: bills up to the amount approved are guaranteed in full, but the Department of Overseas Trade retains recourse against the exporter for 57½ per cent. of any ultimate loss.

(2) Credits in respect of specific transactions, each of which must be submitted to the Department.

The Government guarantees 100 per cent. of bills not exceeding 12 months, and 85 per cent. of others, retaining recourse against the exporter for a substantial proportion of any loss: where the exporter has deposited security, this recourse varies with the amount of the uncovered risk.

The total net guarantees sanctioned amounted at the beginning of 1924 to £10,240,222, of which

£6,220,317 had been taken up; of the latter amount £3,761,868 had been repaid.

### Trade Facilities

Unemployment in 1921 had already become severe, and the next of the contingent liabilities of the Exchequer which we must consider was brought into being in order to tide over the period of re-adjustment to the changed conditions resulting from the war. It was obvious that many capital works which would be of ultimate benefit to the nation were being held over partly on account of the general uncertainty, but partly also on account of the difficulty of raising capital on terms which would make it possible for the works contemplated to operate at a profit. The remedy that was applied was to help industry at home to raise such capital, by lending the credit of the British Government to capital issues. Parliament accordingly authorised the Treasury, on the recommendation of a Committee set up for the purpose, to guarantee the interest or principal, or both, of loans for carrying out any capital undertaking or for the purchase of articles manufactured or produced in the United Kingdom, if the loans were calculated to promote employment. The limit fixed was £25,000,000, but this was increased by an amending Act in the following year to £50,000,000, and a Bill is now before Parliament to authorise a further extension to £65,000,000.

From the latest return issued at the time of writing (H.C. 132 of 1923) it appears that the total of such guarantees sanctioned has amounted to nearly £29,500,000.

The effect of the guarantees is to make any loan

to which they apply a trustee investment in the United Kingdom, and to enable borrowers approved by the Committee to raise money on terms little less favourable than those on which the British Government itself can borrow.

### Austria

Another contingent liability which must be briefly mentioned is the British share of the loan for the reconstruction of Austria. Under the auspices of the League of Nations issues were made by the Austrian Government in the principal financial centres of the world, each of which is guaranteed in fixed proportions by seven nations. The British share of the guarantee is 24½ per cent. and the Exchequer therefore has a potential, though we may already add a remote, liability for this share not only of the sterling "slice" of the loan but also of the dollars raised in the United States of America, the francs in Paris, lire in Rome, and so on; the total amount raised was equivalent to about £27,000,000, and our share of the guarantee is therefore some £6,120,000.

### The National Debt Commission and some others

We have had a good deal to say already about the work of the National Debt Commissioners, and we shall have a good deal more to say about it in connection with the Sinking Funds. It will be convenient here to describe the general nature of their functions, which are in practice discharged by the Comptroller of the National Debt Office and his staff, at their office in Old Jewry. Their chief

function is to receive whatever money any Government departments may have for investment, and to invest it for them. A catalogue of the funds with which they deal in this way will show the great variety of the work which they do. They receive and apply the Old and New Sinking Funds (to be dealt with hereafter), they sell and pay life annuities, they control the Local Loans and Irish Land Purchase Funds, they receive and invest the funds of the Post Office and Trustee Savings Banks, of the Friendly Societies, and last, but not least, of the National Insurance Commission. These are some of their chief occupations; they have many minor ones. Amongst their numerous occupations, the chief in financial importance is their dealing with the funds of the Post Office Savings Bank and of the National Insurance Commission. Because of the big sums involved, they deserve a more particular description.

Big sums are paid every year by the lower and middle classes into the Post Office Savings Bank at local post offices. The Post Office keeps their money for the depositors, and pays them a little interest on it—2½ per cent. Until they want to draw it out, the Post Office has to do something with the money, as any banker would have to do. It hands it over to the National Debt Commissioners for investment. The National Debt Commissioners keep the accounts of the funds of the Post Office Savings Bank. Out of the deposits, as they are paid in, a balance of about £100,000 is kept in the hands of the Postmaster General, at local post offices, and so on. From that are paid sums withdrawn from time to time by depositors. Normally more is paid in than out, and the total balance held has slowly

grown. In prosperous times it used, before the war, to grow at the rate of about £2,000,000 to £3,000,000 a year. The period 1914–1918 was responsible for an increase of £44,000,000, and the year 1919 for a further £32,000,000 due in part to the payment of war gratuities. Since 1920 the normal growth has been counteracted by withdrawals due mainly to unemployment, and there has been little alteration. The excess of deposits over withdrawals is handed over from time to time by the Post Office to the National Debt Commissioners for investment. They are allowed to invest the funds in any stock charged upon the Consolidated Fund, or guaranteed by Parliament. If so be that the withdrawals exceed deposits, the Commissioners of course have to sell stocks and pay over the proceeds to the Post Office; but that happens as a rule only in times of depression and unemployment; the normal state of affairs is a steady growth of deposits, and a steady buying of investments on behalf of the Fund. Interest received on the investments goes to paying interest to the depositors and the expenses of administration, and to making good any depreciation in the capital value of the investments. Any deficiency in these charges left over after using up all the interest received is to be made good by a grant of Parliament out of the Consolidated Fund. Conversely, any excess is to be paid into the Exchequer. The Consolidated Fund is thus liable to make good any amount by which the funds held may prove to be insufficient to meet the claims of depositors in respect of their capital; in other words, the Government guarantees the capital of their deposits.

We have here a constant flow of money through the hands of National Debt Commissioners into

the stock markets for the purchase of Consols and other Government stocks. There are other Government departments which have funds to invest from time to time, and invest them in Government stocks. Chief amongst them are the Currency Note Account, the Public Trustee, the Official Trustees of Charitable Funds, the Supreme Court of Judicature, and the India Office for its Gold Standard and Paper Currency Reserves. Together they make one of the most important groups of customers which buy Government stocks in regular and large amounts; and their proceedings have no little effect on the market therein upon the Stock Exchange.

There is another great stream of money flowing now through the hands of the National Debt Commissioners. It is part of the stream that is always flowing into and out of the National Insurance Fund. Section 54 of the National Insurance Act of 1911 establishes a Fund, the National Health Insurance Fund, into which all contributions received from the insured and their employers and all moneys granted by Parliament are to be paid. It is provided by the Act that sums available for permanent investment are to be paid over to the National Debt Commissioners for that purpose; and any sums in the Fund not required to meet current liabilities are to be dealt with in the same manner. An annual return of the investments so made is rendered by the National Debt Commissioners to Parliament.

The National Debt Commissioners thus act as a conduit pipe through which money is constantly running out of the pockets of depositors in Savings Banks and others, and into those of dealers in Consols and Government stock. There is an aspect of this business of theirs which deserves consideration.

Money in the hands of the Government, as we shall see more clearly in a later chapter, is money that is lying idle. The more the Government has, the less there is to use in trade and commerce. For the sake of trade, it is good that the Government's balances should be as small as possible, and the way for the Government to keep them as small as possible is for the departments to make their disbursements as soon as they can after they have got money to make them with, and to invest as promptly as they can any funds on deposit and any other money for which they have no immediate use. For the latter purpose well-oiled machinery for investment at the National Debt Office is all-important. Were it not to work quickly and smoothly, releasing promptly through the stock markets the enormous and continually increasing sums received on deposit for the Savings Banks and Insurance Commission and other bodies, the Government's balances would tend to be permanently increased, to the detriment of trade.

There is a very useful and practical provision which has been added at times to various Acts of Parliament authorising investment of public funds through the National Debt Commissioners, which helps to keep down balances by prompt investment. It is a provision to enable them to make use of balances of public funds in their hands for investment as temporary advances for certain purposes without waiting for formalities. It has already been mentioned that the Commissioners are empowered to make advances to the Treasury, out of the balances of public funds in their hands for investment, as Ways and Means Advances under the Appropriation Act, in the same manner as the Bank of England. Similarly, the Commissioners are empowered to make

temporary advances out of the funds of the Post Office Savings Bank or the National Insurance Funds to such borrowers as the Local Loans Fund or the Irish Land Purchase Fund. The advance is made by a mere cross-entry in the books at the National Debt Office. If it is not repaid, it has subsequently to be regularised by an issue of stock, such as Local Loans Stock or Guaranteed Land Stock, as security for the advance. The power enables the Commissioners to invest public funds without waiting for the formalities of a stock issue: often the effect of it is that when stock is issued it is merely handed over to the Commissioners as security for an advance already made.

With the National Debt Commissioners' operations on account of the Sinking Funds we will deal in the next chapter.

## Assets

Debt suggests its converse, Assets; and we should not end our consideration of the gloomy liability side of our national balance-sheet without a glance at its brighter side also. It will not delay us long. Tucked away towards the end of the Finance Accounts we find half a page of "Estimated Assets" (excluding Vote of Credit and other War Assets) the total of which was just under £114,250,000 at the end of the financial year 1922–23.

A part of this consists of investments, such as shares in the Suez Canal, and the Anglo-Persian Oil Company; and the bulk of the remainder consists of outstanding loans and advances, to the Unemployment Fund and for Land Settlement, of balances held for special sinking funds, and—the largest individual

item—of the balance of India's voluntary contribution to the cost of the war, which we shall hear of again.

Not included in this list are a few millions of outstanding loans to Colonies and Protectorates for various development works; nor, a far larger item on paper, the war loans to Dominions and Allies and the loans for relief in war areas. These amount in all to £2,095,000,000 of which just under £150,000,000, the loans to Dominions and Colonies, are being repaid as punctually as our own debts.

The war loans to Allies, which represent the bulk of this total, include £601,000,000 due from France, £688,000,000 due from Russia, and £527,000,000 from Italy. Their value as assets we will not attempt to estimate.

Many small States in the Balkans or in Scandinavia could produce a balance-sheet which would look better than that of the British Government. They have Crown lands, forests, and mines of value to set down on the assets side of the sheet, balancing their debts. Nevertheless their credit is not better than ours, and that shows that what a lender thinks about in lending to a State is not what assets it has in hand, but the capacity of its people to pay taxes.

Assets and liabilities make up the nation's capital account. We have now considered how its debt comes into existence, and what it is; and we go on to consider how it is paid off.

# CHAPTER XIII

## SINKING FUNDS

A NATIONAL Debt is like a toothache; it is best of all not to have one, but if you have got one it is next best to get rid of it as soon as you can. Perhaps the harm of having a National Debt is not quite so certain as the harm of having a toothache, but it is certain enough. Of course the economic harm of borrowing money and spending it on an unproductive object, such as a battleship, is obvious. It takes the nation's wealth away from factory, field, and mine, where it would breed fresh wealth, and robs it summarily of all hope of progeny by drowning it in the North Sea. But it is not quite so obvious, once that original waste of capital in the economic sense has been made, that there is any particular harm in allowing things to stay as they are, and in going on paying interest on the capital which has been spent. Interest is paid by taking money out of the pocket of the taxpayer and putting it back into the pocket of the holder of Government securities. All that the payment of interest on internal debt means is that every year a certain amount of money is taken out of the pockets of British taxpayers in general and put back into the pockets of a smaller number of them who are lucky enough to have investments in British Government securities. The nation as a whole is no poorer: what it loses in one place it gains in another. Why then make a great effort to pay

off debt, if we should be none the richer for the repayment?

Of many good reasons for paying it off the best is to maintain the nation's credit. When a nation goes about to borrow, the security which it offers as a pledge to the lender is its taxable capacity. The more debt it has outstanding, the more that capacity is burdened to pay interest, and the less security has the nation left to pledge when it needs a fresh loan. Crises will come, wars and great social reforms, when loans are necessary. Were a nation to make no effort to pay off its debts during the peaceful intervals between the crises, it would find at each crisis that, with less security left to pledge, it had greater difficulty in borrowing, until at last its credit would have become exhausted, and it would fall into ruin and bankruptcy.

A prudent State takes advantage of every lull and interval of peace to pay off debt as fast as it can. It hopes not to have to borrow in future, but it knows that that is a hope for perfection. In course of time it is sure to have to go to the lender again. The more debt that it has paid off during the lull, the better security will it have to offer when that evil day comes, and the better bargain it will be able to make. If it makes no effort, if it allows its debts steadily to accumulate and its general credit to deteriorate, it must ultimately find itself beneath the yoke of the financiers. Several States know that humiliation. By overspending revenue, by contracting debts and not paying them off, and by neglecting to increase taxable capacity by development and good administration, they have brought their credit so low that lenders will no longer trust to their mere promise to repay what is lent. They

ask for a special security, such as the pledge of part of the customs' duties. In a later stage of financial decay, such as that which we see in China, lenders demand that their agents shall themselves collect and control the pledged revenues. In truth a nation which can no longer borrow money on its general credit is no longer wholly free. It falls into subjection to the lenders, and by accepting from them directions as to its policy alienates to them in substance, if not in form, a part of its sovereign rights. It cannot make war or carry out its schemes of development unless the financiers please. It must wait until they choose, and if they demand it, it must let slip from its own hands into theirs a part of its independence before they will allow it to proceed. That State only whose credit stands so high, which has such good securities to sell, that lenders come to it not as givers but as receivers of favour, can consider itself as truly independent.

To the deterioration of credit two things in particular contribute: to borrow when you can do without, and not to pay back when you can. To labour at the repayment of debt whenever times of peace and prosperity make that possible, and to maintain with rigid virtue a liberal provision therefor, are amongst the strongest obligations of patriotic statesmanship. They are also amongst the most difficult to fulfil. There is little popularity to be gained by repaying debt. Nobody feels immediately the benefit of it; that lies hidden in the future. It is fatally easy to divert funds to some more showy purpose, from which somebody with a voice and a vote will get direct benefit. It is easy, but it is disastrous.

So easy is it that it has always been the hardest

thing in the world, even in times of peace and prosperity, to maintain a liberal or even a reasonable provision for the redemption of debt. An annual sum to be applied to that purpose is called a Sinking Fund. During the last century and a half many different sorts of Sinking Funds have been tried, and always a raid upon them has been the favourite expedient of a Chancellor of the Exchequer short of money. Everybody recognises the need of such funds, and almost everybody forgets it as soon as there is the least difficulty in making the two ends of the Budget meet.

"What is the good," says Chancellor By-ends to Prime Minister Halt-by-the-Way, "of keeping up this year such an absurdly large provision for the redemption of debt? So much was never meant to be spent in the service of high and dry financial morality except in an ordinary year—and this is no ordinary year. There is our Better Circumvallation of Cuckoos (England) Act for which money has to be found; or what of the bye-election at Gotham?"

"Very true," says the other; "this year the cuckoos; and next year it will be time enough to get to work on the debt again."

So the Sinking Fund is raided, and when next year comes yet higher walls have to be built round the elusive birds, and the renewal of provision for redemption is postponed to another year.

So notoriously open to attack is provision made to redeem debt that all sorts of schemes have been invented at various times to protect Sinking Funds from raids, either by hiding them or by fortifying them with laws. One of the arrangements for hiding them away from the spoiler is still in use, and we shall

have to deal with it shortly later on. But as to all the others experience has shown that no hiding and no legal protections are of any use. It is idle to try and bind future Parliaments with an Act of Parliament, because what Parliament has done Parliament can undo again whenever it likes. With the wisdom gained from experience, all artificial protections, concealments, and guarantees of the Sinking Fund were at one time abandoned, and the various provisions for the redemption of debt were concentrated into two sums devoted annually to that purpose, called the Old and the New Sinking Funds, which we will consider in turn.

### The Old Sinking Fund

A Government has got no business to get more money out of the taxpayers than it needs for the immediate business of Government, or to keep funds lying idle for which it has no present use. Money is the manure of industry. It should be left to enrich that field; to keep it locked up in the Government's box is to impoverish the nation. Like any other house of business the Government must keep a little carry forward in the form of an Exchequer Balance at the end of the year, and a tiny reserve in the Civil Contingency and Treasury Chest Funds. But it should not allow funds to accumulate in any other way, and in fact it does not. If it is in possession of more funds than are needed for its business, some use should be found for them by which they can be set free again to fertilise industry. Such a use can always be found in the redemption of debt. Public money not needed for any other purpose can be well employed for that, and so it is.

It is not until the end of a financial year that the Government knows how much it will need for the services of that year, or how much it will have with which to meet its need. Not until the end of the year does it know whether it has any surplus funds in its hands; but when on March 31st receipts into the Exchequer Account for the year and issues from it for the year's services have been finished and balanced, then the Government knows whether it has anything left over. If it has, it sets that surplus to the credit of a fund which is called the Old Sinking Fund, because it is older than the New Sinking Fund, and devotes it to the reduction of debt.

It is not the gross balance of the Exchequer Account on March 31st that falls into the Old Sinking Fund, but a part of it only. It is that part which represents the excess, if any, of sums received into the Exchequer Account in respect of public income over expenditure chargeable against that income. In order to make this matter clear to ourselves we must notice that in the record of receipts into the Exchequer Account and of issues from it a difference is made between those on Revenue Account and those on Capital Account. They are recorded separately. First of all the revenue receipts are stated, customs and excise, and so on; and against them as chargeable against revenue is set the expenditure on Consolidated Fund Services and on Supply Services. Then the record proceeds to show other receipts and issues, which are receipts and issues of money borrowed temporarily on capital account. It is only the surplus of revenue receipts over expenditure chargeable against revenue that has no special use provided for it and is free and idle. Capital

receipts are as a rule all allocated to special purposes that do not end with the year, and the surplus of capital receipts over capital expenditure at the end of the year is neither idle nor free. It is therefore only the revenue surplus that can appropriately be applied to the reduction of permanent debt. Were the surplus of temporary borrowings on capital account to be so applied, an equal amount would simply have to be re-borrowed and we should have the absurd result that we were paying back debt with one hand and at the same time borrowing an equal amount with the other.

An analysis of the record of the Exchequer Account at the year's end will help to make clear the nature of the surplus credited to the Old Sinking Fund. The figures given are those for 1912–13.[1] At the end of that year the record of the Exchequer Account may be summarised as follows:—

ANALYSIS OF EXCHEQUER RECEIPTS AND ISSUES, 1912–13.

| | | | |
|---|---|---|---|
| **Revenue.** | | | |
| | £ | | £ |
| Revenue Receipts ... ... ... ... | 188,802,000 | ... | |
| Expenditure chargeable against Revenue ... ... ... ... | 188,622,000 | | |
| Surplus ... ... ... ... ... ... | 180,000 | ... | 180,000 |
| **Capital.** | | | |
| Other Receipts ... ... ... | 42,625,000 | | |
| „ Issues ... ... ... ... ... | 47,945,000 | ... | |
| Deficit ... ... ... ... ... ... | 5,320,000 | ... | 5,320,000 |
| | | Net Deficit | 5,140,000 |
| Balance in Exchequer 1912, April 1st | | ... ... | 11,469,000 |
| Balance in Exchequer 1913, March 31st | | ... ... | 6,329,000 |

[1] See p. 279.

Revenue receipts consist of customs, excise, income tax, etc. Expenditure chargeable against revenue consists of Consolidated Fund and Supply Services. Other receipts and issues, on capital account, consist of all the transactions in respect of Treasury Bills, Terminable Annuities and the rest of them. Our analysis shows that there was no surplus of total receipts over total issues. Total issues exceeded total receipts by £5,140,000, so that Exchequer Balances were reduced by that amount. But revenue receipts exceeded expenditure chargeable against revenue by £180,000. That surplus of £180,000 was the sum that on March 31st, 1913, was automatically credited to the Old Sinking Fund.

On March 31st at 4 p.m. the balance of the Exchequer Account is struck, and the surplus to be credited to the Old Sinking Fund, if any, is immediately ascertained. It is immediately ascertained, but it is not immediately issued. It may be left for long months swelling the Exchequer Balance. According to the Sinking Funds Act of 1875 the Treasury may issue it from the Exchequer Account for the redemption of debt at any time it pleases in the course of the next financial year. Often it does not issue it until the last quarter of that year, more than nine months after its amount was ascertained. When the Treasury considers that the time has come to make use of it, it issues it all at once or in instalments to the National Debt Commissioners, and they employ it for the reduction of debt in a manner to be described shortly. They must use it all up within six months of the time at which it was issued, so that a part or the whole of it may still be in their hands unspent at the end of

the financial year following that in which it came into existence. They may apply it to buying or redeeming any Government stock the interest of which is charged directly and primarily on the Consolidated Fund. It is provided by the Treasury Bills Act of 1877 (§ 7) that they may also apply it to the purchase of the renewable (Supply) Treasury Bills. Another and the only other purpose to which it may be applied is the repayment of Deficiency Advances made by the Bank of England under the Exchequer and Audit Act. It may not be applied to the repayment of Ways and Means advances made under the annual Appropriation Act, nor may it be applied to the purchase of Ways and Means Treasury Bills issued under that Act.

The surplus which is credited to the Old Sinking Fund is sometimes confounded with the balance of savings which is surrendered by the departments. They are not the same things: there is in fact no direct connection between them. The surplus for the Old Sinking Fund is what we have seen. It is the excess at the end of the financial year of revenue receipts into the Exchequer Account over issues therefrom chargeable against revenue. It is ascertained when the Exchequer Account for the year is closed on March 31st. The surpluses to be surrendered by the departments are the savings on their grants, which are the sums by which their actual net expenditure on the grants falls short of the grants themselves. They are not ascertained until the Appropriation Accounts are made up several months after the close of the financial year. The surplus for the Old Sinking Fund is represented by credit still in the Exchequer Account, and it stays there as part of the Exchequer Balance until

it is issued by the Treasury to the National Debt Commissioners; surpluses to be surrendered by the departments are represented partly by credit still on the Exchequer Account and partly by credit in the hands of the Paymaster General and of sub-accountants. Departmental savings do indirectly affect the surplus available for the Old Sinking Fund, but not always the surplus for the year in which they were made. They affect that surplus only if the Treasury makes a short issue. If the Treasury is sure (as it seldom is) that the net expenditure of a department on a certain Vote will be less than the amount granted for that Vote, it leaves some of the amount so granted unissued from the Exchequer Account at the close of the financial year. That decreases the total issues for the year chargeable against revenue, and thereby increases the surplus, if any, for the Old Sinking Fund. On the other hand if the whole amount of a grant for a Vote is issued to a department, any saving which it finds that it has made when it draws up its Appropriation Account is repaid to the Exchequer by being written off the grant for the similar Vote in the year then current. The effect of that is to decrease the issues from the Exchequer chargeable against revenue, and thereby to increase the surplus (if any) available for the Old Sinking Fund, in the year following that to which the saving belongs. It follows that the Treasury can within limits manipulate the Old Sinking Fund. Suppose that towards the end of the financial year it sees that there is going to be a big surplus for the Fund, and suppose that in part that surplus is due to departments having been so economical that it will be possible for the Treasury to leave

the financial year following that in which it came into existence. They may apply it to buying or redeeming any Government stock the interest of which is charged directly and primarily on the Consolidated Fund. It is provided by the Treasury Bills Act of 1877 (§ 7) that they may also apply it to the purchase of the renewable (Supply) Treasury Bills. Another and the only other purpose to which it may be applied is the repayment of Deficiency Advances made by the Bank of England under the Exchequer and Audit Act. It may not be applied to the repayment of Ways and Means advances made under the annual Appropriation Act, nor may it be applied to the purchase of Ways and Means Treasury Bills issued under that Act.

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provided every year more certain in amount. At bottom the object of making provision of the sort is to maintain the nation's credit amongst lenders. Nothing is more encouraging to a lender than to see his debtor paying off debt with reasonable rapidity and with absolute regularity, according to a fixed programme. It was not until 1875, when Sir Stafford Northcote (Lord Iddesleigh) was Chancellor of the Exchequer, that the need for a fixed annual provision for the reduction of debt in general was recognised, to supplement the Old Sinking Fund and to take the place of a number of minor and special sinking funds. In that year was established a permanent or fixed annual debt charge. The principle of this charge was that it should not only cover the entire service of the debt, but also leave a margin which would be applicable to redeem capital, and which would automatically grow as the other charges fell owing to the decrease in interest as debt was reduced. This margin was what has since been known as the New Sinking Fund. The amount of the fixed debt charge, originally fixed at £28,000,000, was altered from time to time, notably in 1887–88, and 1889–90 to £26,000,000, and £25,000,000, and in 1899–1900 to £23,000,000. At the beginning of the war it stood at £24,000,000, of which the New Sinking Fund amounted to £5,228,000.

The service of the new debt created for the purposes of the war was never brought within the fixed debt charge, and it therefore became necessary to reconsider Sinking Fund policy as soon as the amount of that debt became sufficiently fixed. There were two alternatives: (1) to leave the principle of the Act of 1875 unaltered, and merely to increase the amount of the fixed debt charge; (2) to do away

with the fixed charge and to provide a separate Sinking Fund. For various reasons the latter alternative was chosen, and the Finance Act of 1923 established the "New Sinking Fund, 1923," amounting to £40,000,000 in 1923–24, £45,000,000 in 1924–25, £50,000,000 in 1925–26, and in every subsequent financial year unless and until Parliament otherwise determines.

The whole amount must be issued within the financial year, and must be "applied within nine months after the date of issue thereof in the purchasing, redeeming, or paying off of debt charged on the Consolidated Fund . . . other than advances made by the Bank of England or the Bank of Ireland under section 12 of the Exchequer Account Act, 1866, or loans raised under any Act to meet Ways and Means."

It will be seen that the New Sinking Fund, 1923, like the New Sinking Fund which preceded it, but unlike the Old Sinking Fund, cannot be used to repay Deficiency Advances.

We have now dealt with the differences between the Old and the New Sinking Funds. Next we will deal with what is common to both, and that is the way in which they are applied. In each case credit is issued from time to time on account of that part of the Sinking Funds which is to be applied to the redemption of internal debt by the Treasury to the National Debt Commissioners. It is applied, for the most part, by buying stock in the open market on the Stock Exchange. To make their purchases for them the Commissioners employ a long-established firm of stockbrokers of high standing, who are commonly known on the Stock Exchange as the "Government brokers." Credit is issued to the Commissioners by the Treasury in large amounts.

Needless to say it is not all applied to the purchase of stock at once and in a lump. Acting under the instructions of the National Debt Commissioners and in the light of their professional skill and knowledge of the Stock markets, the Government brokers make their purchases gradually and according to the state of the market. Pursuing the obvious end of getting as much stock for as little money as possible, they buy more when the price is low and less when the price is high, and always a little at a time, so as to avoid raising the price of the stock against themselves by running the market short of supplies. Of course the frequency and the amount of their purchases depend on the amount which they have to spend.

In these appearances of the Government brokers on the Stock Exchange and in their purchases there we see actually at work the process of maintaining the credit of the nation by the redemption of its debt. The object of maintaining its credit is in order that, if it has to borrow again, it may be able to do so easily and cheaply. Ease and cheapness in borrowing depend on the market valuation of the Government's outstanding stock; the lower the price of Government securities the more expensive is it for the Government to borrow. If, for example, the market price of £100 nominal of Consols is £90, the Government would get £90 or a little less for a new promise to pay £2 10*s*. a year; if it is only £80, that is all that the promise would fetch. In other words to maintain its credit as a borrower the Government must maintain the price of its issues. Now this depends in the first place on the total supply of capital for investment and the demand for it, and those are things too big to be controlled

by the measures even of the British Government. But they depend also to some extent on the supply of Government securities, and on the demand for them amongst investors. The bigger the demand and the less the supply, the higher the price. So although the Government cannot absolutely control the price of its stocks, which depends mainly on the state of affairs in the world's capital-markets, it can do something to help to maintain that price by reducing the supply and increasing the demand. That is what it does by setting aside money for the Sinking Funds and by keeping the Government brokers busy buying the stock in the open market. Their purchases have a very decided effect in checking a fall, and in hastening a rise.

Since a mistake is often made about the matter, it is worth while specially to mention that neither Old nor New Sinking Fund can be applied to the buying of Local Loans or of Guaranteed Irish Land Stock. Only those stocks can be bought with these funds which are directly charged upon the Consolidated Fund, and Local Loans and Land Stock are charged upon it indirecctly and contingently only. Each of those stocks has its own arrangements for redemption. Instalments of the principal of Local Loans are repaid by the local authorities to the Local Loans Fund. They are used, not indeed for the redemption of Local Loans Stock, but to keep down the issues of fresh stock required, by providing funds for fresh loans to local authorities. It is obviously sound policy that the instalments of capital should be used rather as a means of reducing the amount of fresh issues of stock than to buy stock in the market; it would be foolish waste of money to pay commission to brokers

for buying stock and selling stock at the same time, when the money can simply be taken and used without any stock operations at all.

When the National Debt Commissioners have bought stock with money from the Sinking Funds, they cancel it by an entry in the registers kept at the Bank of England, and that is the last stage in the process of reducing the National Debt. A little help in the work of reduction is had from one or two other sources. In imposing certain taxes, particularly the Land Tax and certain Stamp Duties, Parliament has allowed those liable for the taxes to compound for their periodic payment by a single payment. A payment of the sort is a capital payment made once and for all instead of a payment made annually or at other intervals. It ought therefore not to be spent as revenue. It ought to be invested, and it is. In giving leave to compound payments of the sort, Parliament expressly provides that the money received for composition is to be invested in the best investment for the Government, which is its own stock. The money is paid over to the National Debt Commissioners, who buy Government stock therewith and cancel it.

Another way in which Government securities are withdrawn from the public is the payment of death duties, etc., in stock. We saw in Chapter X. that some of the war issues are accepted in payment of these taxes, and the stock so tendered is forthwith cancelled (except in the case of Victory Bonds, which, since cancellation would disorganise the drawings for redemption, are held by the National Debt Commissioners until they are drawn).

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at the last moment or, if they could, the sterling-dollar exchange and consequently the cost of the dollars might go to almost any figure; it is therefore essential to buy the dollars over a period of months, mainly of course at the times when from seasonal or other causes the exchange is relatively favourable to this country.

There is a principle which underlies the scientific use of Sinking Funds obvious enough when it is set down in black and white, which yet took the official financiers of this country a long time clearly to understand, and which those of some other countries seem not to understand yet. We have already referred to it more than once. It is the principle that it is no use to reduce debt with one hand if at the same time you are increasing it with the other. From the point of view of the stock market the principle may be expressed thus: that it is no use to increase the demand for Government stock if at the same time you increase the supply. Whatever good effect the increased demand would have had on the price is negatived by the ill effect of the increased supply. Suppose that a Government has set aside out of revenue £5,000,000 a year for its Sinking Fund for the reduction of debt; and suppose that a year comes when to make revenue balance expenditure it needs £5,000,000. It may if it pleases still pay the £5,000,000 into the Sinking Fund and redeem debt with it, and borrow a fresh £5,000,000 to make both ends meet. Sometimes in the past that has been done, or at least something practically equivalent to that. It has been argued that it would have a bad effect on the price of Government stock to stop the purchases for the Sinking Fund. So it

would; but the effect of creating £5,000,000 of fresh debt is just as bad, in quantity and quality. Under the sorry circumstances the only sensible thing to do is to raid the Sinking Fund, to use the £5,000,000 to meet expenditure, and to leave the debt unreduced on the one hand and unincreased on the other. That is the more economical course, because it saves the expenses both of paying off and of creating £5,000,000 of debt. It has another positive advantage: it keeps the nation's accounts free of artificial cross-entries, and prevents the unwary from deluding themselves into the belief that the nation has made a true reduction of £5,000,000 in its total debt. It makes no difference whatever that there is some distinction in the class of debt redeemed and created; that the one is temporary, for instance, and the other permanent. On the nation's credit the result is in the long run the same.

To raid the Sinking Fund is the best thing to do under the circumstances; but that does not make the circumstances any the less evil. Once a fixed annual sum has been set aside for a Sinking Fund, every conceivable effort, for reasons already given, should be made to maintain the provision. It should be looked upon as an absolutely binding obligation. Only if, under compulsion of extreme necessity, the nation has been forced to overspend its income, it is better for it to draw upon the Sinking Funds to make both ends meet, before it borrows afresh. For the nation to maintain the operation of a Sinking Fund at a time when it is creating fresh debt is always wasteful, and always tends to conceal the true state of its finances. A State should by all means strive to make its revenue balance its expenditure, with something over for the

reduction of its debt. If it fails to do so, it is starting on a race with the constable; but to try to conceal the constable's pursuit by an ostentatious reduction of debt which is negatived by a simultaneous increase is but to give wings to the pursuer's feet.

It used to be thought good policy as far as possible to tie up Sinking Funds and tuck them away in corners to protect them against depredations. No concealment, however, was found to be of any use against a Chancellor in a bad scrape for money. As the principle, moreover, became more clearly understood, that it is no use to pay off debt with one hand whilst you are creating it with the other, it became clear also that there was a positive disadvantage in having Sinking Funds too carefully tied up and hidden. It meant that in a bad year, when fresh debt had to be created, the Sinking Funds could not be readily untied and used to help the revenue and to reduce the amount of fresh debt to be created, as they ought to be. For that reason, men found, it was better to have the whole provision for the reduction of debt concentrated in the Old and New Sinking Funds. It is there in the public eye and has the only protection that in the long run is much help to a Sinking Fund, and that is public opinion; and when fresh debt has to be created, it can be emptied back into revenue to keep down the amount of fresh debt without disturbing other regions of the financial organisation.

For these reasons we must regard it as unfortunate that, as we saw in Chapter X., some of the British Government loans during the war were issued with special Sinking Funds. It is true that this device, by making the maintenance of a Sinking Fund part

of the bargain between the Government and the investor, does effectually tie up the Sinking Fund provision and make it impossible for any Chancellor of the future, whatever his need, to raid it without a definite breach of faith. But this intensifies the disadvantage just mentioned that when a new need arises the then Government will be borrowing to pay off debt; and in the event of heavy future borrowing for such a crisis as another war, it would have the effect of favouring some Government securities at the expense of others.

### Annuities for the Reduction of Debt

We have with us one survival from the old days of special Sinking Funds. There used to be a very favourite way of tying up a Sinking Fund and tucking it away. It was invented by Gladstone in 1863. When it was found that there was a large block of Government stock in the hands of a public department as an investment for public funds, the Government took the stock, cancelled it, and gave the department a terminable annuity instead. It paid the department interest equivalent to the interest on the stock, and paid to it every year in addition an instalment in respect of capital. The department, as it received the instalments in respect of capital, invested them in fresh stock. When the instalments of capital had all been paid by the Government to the department, the terminable annuity had come to its termination. The whole result of the transaction was that a block of stock had been cancelled, that the department had been repaid its capital value, had invested it in fresh stock, and had received interest in the

meanwhile. So the effect of the terminable annuity was to act as a little special Sinking Fund for the reduction of debt by the amount of the particular block of stock cancelled.

Arrangements of this sort were made through the National Debt Commissioners, and the stock in respect of which they were made was mostly Government stock held as investments on account of the Savings Banks. One such terminable annuity is still being paid and will not terminate until 1924–25. It was created in 1900 to cancel £15,000,000 of Consols held as an investment for Savings Bank Funds. There is another still being paid that expires this year (1924). It was created in 1900 to extinguish a debt of £13,000,000 due from the Government to the Savings Bank Funds. This debt was represented by no securities, but by a mere entry in the books of the Treasury. It was for that reason called a Book Debt, and the annuity to extinguish it is called the Book Debt Annuity. The Book Debt, charged upon the Consolidated Fund, was brought into existence in 1893, in substitution for £13,000,000 of Unfunded Debt, which was then cancelled.[1]

Terminable Annuities for the reduction of debt fell into disuse after the establishment of the New Sinking Fund. Content with the provision made by the latter for the reduction of debt in general, Parliament no longer exerted itself to reduce this or that debt in particular. But in their days these terminable annuities did good work in the reduction of debt, and in helping the process of converting Consols from a 3 per cent. to a 2½ per cent. basis.

[1] There is also a small Sinking Fund Annuity of £15,500 terminating in 1934 which is the remains of a conversion operation in 1884.

## CHAPTER XIV

### THE GOVERNMENT, THE BANK, AND THE CITY

THE Bank of England is not a Government office. It is established by Acts of Parliament, but so is the Great Western Railway. It does work for the Government, but so do Messrs. Armstrong, Whitworth & Co., the manufacturers of armaments. Neither of those things make it in any sense an official body. It is not even a State bank under the direct supervision of the Government, like the Bank of France. It is a private banking company, governed by a court of merchants of the City of London which is elected by the shareholders. Its capital has been privately subscribed in the past, and is held now by private persons; its shareholders are thus a private body, and the court which they elect is their private committee, and legally responsible to themselves alone. It is on their behalf alone that the business of the bank is conducted, earning for them a comfortable dividend on their stock.

It is true that the Bank of England cannot and does not behave quite as if it had no interests to consider other than those of its shareholders. A monopoly has been conferred upon it by Act of Parliament, to be the only bank in London that may issue paper notes. The effect of that is to make it, not indeed a State bank, but the central

bank of the country. As Walter Bagehot proved in his classical work, *Lombard Street*, a central bank with sole power amongst banks to issue notes has duties towards the banking and commercial communities, and through them towards the country at large, which it is bound to perform in return for the privileges given to it. In banking matters it must look upon itself as a public body with public work to do. But those obligations of the Bank of England concern banking matters only; they have no direct relation with the organisation of the finances of the Government, and that is the only subject with which we need deal here. As far as that organisation is concerned, there is only one thing in connection with the Bank of England which requires our attention; it happens to be the bank which has the Government for customer.

## The Bank

As the private person banks with Lloyds or Barclays, so the British Government banks with the Bank of England. Private persons may and do bank there too, if they are rich and respectable enough; the British Government is only the richest and most respectable of the Bank's numerous customers. The services which the Bank performs for the Government are not much different in nature from those which any bank performs for any private customer. What our banker does for us is to take care of our money when we are lucky enough to have any. What money we receive we hand over to him, and when we want some of it back we get it from him by a cheque. He keeps an account for us, showing how much we have paid in and how much we have

drawn out and what we have left. That is in substance what the Bank of England does for the Government. It receives the Government's revenue, pays out money for it under the direction of the Paymaster General, keeps its balance for it, and records all these transactions in books of account.

Besides such regular banking work, it does another piece of work for the Government which is not that of a regular banker; it manages the Government's Debt. It keeps the registers of its stocks, arranging for their transfer from one name to another as they are bought and sold; and it pays their dividends to the stockholders.

Good arrangements for transferring stocks are a very necessary thing, and the services which the Bank performs for the Government in that matter are not the least important which it renders. The more easily and promptly a stock is transferable, the more desirable it is to investors; one thinks twice before buying a stock if one has any doubt about being able to sell it readily to somebody else when one wants the money. So on the excellence of the Government's and the Bank's arrangements for their transfer depends, to some extent, the market price of Consols, which is a measure of the rate at which the Government can borrow.

These are the Bank's chief works in connection with the Debt; in addition it manages fresh issues of stock, including the issue and repayment of Treasury Bills and Exchequer Bonds. With these matters we have dealt in past chapters, and with the manner in which the Bank grants temporary advances to the Treasury. If we add that the Bank is the medium for the issue of currency and the withdrawal of light coin, that completes the catalogue

of the work which it does for the Government. For doing it it receives remuneration at a rate which is fixed by various statutes. Part of its reward is that it pays no interest to the Government on the balances of public money which it holds from time to time. In this matter the Government is on an equal footing with the Bank's other big clients, a class which includes all the big joint-stock banks of the country. To none of them does it pay any interest on their deposits. The Government, moreover, gets from the Bank no security for its deposits, as a depositor would get in less exalted regions of finance.

As depository of the public funds the Bank keeps the banking accounts of the departments, receives their revenue for them as it is paid in, pays their drafts, and holds their securities for them, including those held by the National Debt Commissioners. We have dealt in past chapters with some of the principal departmental accounts at the Bank, especially those of the Boards of Customs and Excise and of Inland Revenue, and those of the Paymaster General. But no full or detailed information is available for the public as to the number and nature of the accounts kept by the Bank for the public departments. That is treated as a private matter which concerns only the departments and the Bank.

As it is, all that we know about the state of the balances of public money at the Bank is told us in the Bank's statutory return of its assets and liabilities which is published every Thursday. That shows amongst the items of the Bank's liabilities one called "Public Deposits." It varies widely. It is usually at its lowest about October, after the quarterly

payment of interest on the debt, and rises during the last quarter of the Government's financial year, when the revenue is flowing in freely, to reach its maximum in the last week in March.

"Public Deposits" are the money which the Government has at the Bank. They include all the balances at the credit of any department of the British Government, and none other. In particular they do not include, as is sometimes supposed, the balances held by the Bank for the Government of India or for the Agents General of the Colonies, or for any Dominion Government, or for the London County Council, or for any other municipality or local authority. Public Deposits, the total of which is stated in the Bank Return, are the money of the Government departments only. First in importance is the balance on the Exchequer Account, which is under the control of the Treasury and of the Comptroller and Auditor General. That is Government money in a state of equilibrium, safe under the thumb of the Treasury and Parliament. Next in importance and at times greater in size is the balance of the Paymaster General on those accounts of his which have been described in an earlier chapter. That is Government money on its way out from the Exchequer Account to the Government's creditors. Then there are the balances in the hands of the Board of Customs and Excise, on accounts also described in an earlier chapter, and those in the hands of the Board of Inland Revenue. They are Government money on its way into the Exchequer Account from the pockets of the taxpayers. Substantial in amount also are the balances in the hands of the National Debt Commissioners, for the most part awaiting investment. The Post

Office, the Supreme Court of Judicature, and others also have at most times substantial balances of public money standing to their credit at the Bank of England. All these together make up the Public Deposits in the Bank Return.

For reasons which we will go into a little later the financial community is interested week by week carefully to observe the amount of the Public Deposits. In the course of its observations it sometimes allows itself not clearly to distinguish between Public Deposits and Exchequer Balances. Exchequer Balances are shown by the Treasury's Return of National Income and Expenditure, which records the state of the Exchequer Account on Saturday, and is published in the *London Gazette* every Tuesday. Public Deposits are shown by the Return of the Bank of England, which records the state of its assets and liabilities on Wednesday, and is issued every Thursday. To one, faint but pursuing, who has read so far as this, it will be clear that there is little or no direct relation between the two. Some public moneys appear as Public Deposits and disappear again without ever entering the Exchequer Account at all. We have seen how some slips on to the accounts of the Revenue departments and on to the cash account of the Paymaster General at the Bank and slips off again, dodging the Exchequer Account altogether. Again, credit issued from the Exchequer Account to the Paymaster General may remain on his accounts at the Bank for some time before it is finally transferred to the Government's creditors. By the issue of that credit from the Exchequer Account to the Paymaster General Exchequer Balances are depleted, but as long as it remains in the hands of the

Paymaster General, Public Deposits are undiminished. There is therefore no necessary correspondence between minor increases and decreases in Exchequer Balances and Public Deposits. When big issues are being made from the Exchequer Account and are being rapidly disbursed by the Paymaster General on account of the departments, as at the end of a quarter, the two visibly decrease together, and when the revenue is being rapidly collected and credited to the Exchequer Account the two visibly increase together; but at other times their movements up or down are not necessarily simultaneous.

There is thus little complexity in the relations between the Bank of England and the Government. The Bank looks after the Government's balances for it, and keeps a record of payments in and payments out. It makes those payments as it is directed by the Treasury or by the other department on whose account they are made. In all its work for the Government and for the departments its duties are purely ministerial. It does the work which any other banker might do, and no more. Nor has it any duty towards the public in these matters. Its only duty is towards the officers of the Government, who are its customers. Neither the public nor Parliament can take the Bank to task for anything which is found amiss. They must take to task their own ministers and servants in the Government and the departments.

Bank and Government have always pulled well together, nor is there record of any grave differences between them. The nation has had no complaints to make. Were it to be otherwise, in the last resort the State could change its banker. It would take an

Act of Parliament to do it, but it could be done. Things, however, are excellently well as they are, and so subversive an idea is only mentioned here in order to lay stress upon the purely private position of the Bank in our scheme of State finance. Theoretically another and a more obviously private bank could do the work which the Bank of England does for the Government without any fundamental change in our system.

## The City

Through the Bank of England the process of getting and spending the Government's revenue is of intimate concern to the great financial community which has its being in the City of London, and through that community it concerns the country as a whole. Of course the collection of taxes makes itself felt upon the individual taxpayer; he feels it because he has to draw a cheque. That is a direct and obvious effect of the ingathering of the revenue. But there is another effect of it, less direct and less obvious, which nevertheless makes itself felt year by year in a very decided way upon the country and its trade. Since this is a point at which a large class of private citizens feels directly the working of the State's financial machinery it is worth while to trace the matter out with some particularity.

Our public revenue amounts now to about £800,000,000 a year, and in addition to that there is a substantial annual turnover on account of capital. Anybody might guess that this big sum could not be taken out of the nation's pocket without the process having some marked effect on the nation's private business. Nor can it. Money is the life

blood of trade and industry, and the more of it that the Government collects and keeps by it, the less active can trade and industry be. It is true that the millions of revenue and capital are not destroyed. They are all paid back to somebody or other in the course of the year, and since getting and spending go on simultaneously it is only a small part of the total that is in the hands of the Government at any given time. But that part is great enough to make a good deal of difference to the trade of the country, and even of the world, in the manner which has now to be described.

In a previous chapter an account was given of the way in which the revenue is collected. Little cash changes hands. By means of cheques tax-payers transfer a part of the balances which stand to their credit at their banks to the credit of the Government at the Bank of England. Now it so happens that the banks of this country, like the Government, themselves bank with the Bank of England. That has nothing to say to the Bank of England's position as the Government's banker. It is due to its position as the central bank of the country, which keeps the country's gold reserve. Just as each of us keeps a little of his money in his pocket for daily needs and deposits the rest with the Westminster Bank, it may be, so the Westminster Bank keeps a little cash in its till, and deposits the rest of its money with the Bank of England. If we look at the weekly Bank Return, we shall see upon the "liabilities" side an item called Other Deposits. Of this the greater part consists of the balances of the banks of the country, deposited by them with the Bank of England.

When we pay our taxes, we transfer to the

Government by means of a cheque a part of the balance which we have at our bank. Our bank makes the transfer for us by transferring an equivalent part of its balance at the Bank of England to one or other of the Government accounts there. The credit transferred then disappears from the Other Deposits, and being set to the account of one of the departments of the Government and ultimately to the Exchequer Account, appears on the Public Deposits.

Now Public Deposits at the Bank lie idle. Neither the Treasury nor any other Government department nor the Bank on its behalf makes any use of them. They are credit which is not available for trade or any other purpose until it is paid out again and released.

On the other hand the bankers' balances at the Bank of England, making up the greater part of Other Deposits, are the chief constituent of the fund out of which are provided the daily needs for money of the trade of this country and of a great part of the civilised world. Every day in the year the merchants and financiers of the world borrow a lot of money in the London money market. They borrow the money by discounting bills, selling a promise to repay £100, say, on a certain future day for £100 $-x$ pounds paid to-day to the seller of the promise. $x$, called the discount rate, is a rate of interest on the money paid for the promise, for the period between the present date of its payment and the future date at which it will be repaid.

Every day as these bills mature the merchants and financiers of the world pay back a lot of the money which they have borrowed.

It is from the bankers of the country that the

blood of trade and industry, and the more of it that the Government collects and keeps by it, the less active can trade and industry be. It is true that the millions of revenue and capital are not destroyed. They are all paid back to somebody or other in the course of the year, and since getting and spending go on simultaneously it is only a small part of the total that is in the hands of the Government at any given time. But that part is great enough to make a good deal of difference to the trade of the country, and even of the world, in the manner which has now to be described.

In a previous chapter an account was given of the way in which the revenue is collected. Little cash changes hands. By means of cheques taxpayers transfer a part of the balances which stand to their credit at their banks to the credit of the Government at the Bank of England. Now it so happens that the banks of this country, like the Government, themselves bank with the Bank of England. That has nothing to say to the Bank of England's position as the Government's banker. It is due to its position as the central bank of the country, which keeps the country's gold reserve. Just as each of us keeps a little of his money in his pocket for daily needs and deposits the rest with the Westminster Bank, it may be, so the Westminster Bank keeps a little cash in its till, and deposits the rest of its money with the Bank of England. If we look at the weekly Bank Return, we shall see upon the "liabilities" side an item called Other Deposits. Of this the greater part consists of the balances of the banks of the country, deposited by them with the Bank of England.

When we pay our taxes, we transfer to the

are at times so very big. In the first three quarters of the year, the bankers who lend and the merchants and others who borrow are little affected by the state of Public Deposits. From week to week their amount does not change enough to make much practical difference. But in the last quarter of the financial year it is quite another matter. It is then that the tax collector "comes amongst us, having great wrath because he knows that his time is short." Taxes in general, and the income tax in particular, are being collected speedily and without mercy. Public deposits mount up by leaps and bounds. The withdrawal of so large a sum as that, from the fund out of which daily borrowings and lendings are made for commercial purposes, makes a very practical difference to lenders and borrowers. Commonly it has the result of making borrowers decidedly hard up for funds, particularly when Public Deposits are approaching their maximum in March, and of raising in consequence the discount rate. Then when March 31st comes, big disbursements are made by the Government, Public Deposits fall back to a more normal level, Other Deposits rise in proportion, the fund for loans is replenished, and the discount rate tends to fall.

To finish our account of the relations between the Government's financial proceedings and the money market, we may observe that fluctuations in the total amount of Treasury Bills outstanding have a similar effect on borrowers and lenders. Paying for them on issue decreases the funds available in the market, and tends to raise the discount rate. When they are repaid the funds available for use in the market are increased, and that tends to the reduction of the discount rate.

The accumulation of credit on Public Deposits in the last quarter of the financial year is of a good deal of advantage to the Bank of England, and in several ways. In the first place it enables the Bank to earn bigger profits. By depleting the funds available for use in the money market, it enables the Bank to charge more for what it has to lend. It also brings custom to the Bank. When supplies of credit are running short, and other lenders, banks and so on, have got nothing left to lend, it is to the Bank of England, as the central bank and the keeper of the nation's gold reserve, that borrowers have to come in the last resort. In February and March, when Public Deposits mount high, it is common to find borrowers flocking to the Bank for loans, and the Bank makes a very nice profit out of lending to them. In general, the scarcity of credit in the London money market which the ingathering of the revenue often produces for a month or so is a very useful help to the Bank in its function of controlling the money market.

Such temporary and artificial reductions in the supply of credit are on the other hand bad for borrowers who, because of them, have for a time to pay a higher rate of interest. On the whole they are a positive evil. Capital is the raw material of every industry; the more and the cheaper it is the greater the industrial activity of the country. It is then a part of good government to avoid making credit scarcer and dearer by such temporary accumulations of money in the hands of the State. We return here in our last pages to a principle which was stated in our first, that a Government has no business to take out of the pocket of the taxpayers and keep lying idle more of their money than is absolutely

necessary for its immediate purposes. All possible measures should be taken to keep Public Deposits at all times as low as possible. Care in that is more needed every year. The business of government and the number of the State's activities steadily grow, and with them grow the size of the revenue and of the various funds with which the Government has to deal. Under these conditions, without constant vigilance to prevent it, there is some danger that an increasing burden may be cast upon the industries of the country by the accumulation of an increasingly large balance on the Government's accounts.

We may conclude with a summary of this matter. Public Deposits are an evil because they make the country poorer. If they are no bigger than the Government needs, then they are a necessary evil; but if the Government's needs are exceeded, then they are an evil that is unnecessary. Variations in Public Deposits are an evil because they disturb trade. Small variations are inevitable, but a big and violent variation, such as that which comes at the end of the financial year, can and ought to be made much less.

And, by way of a final winding up, we may stretch that to a wider generalisation. All the financial operations of the State are an unmitigated evil, which is, unluckily, necessary. It is an evil, although a necessary one, that the State should have to collect and spend a revenue. A tax is a bad thing and not a good thing. It reduces the incentive to work and save; it diverts money from its natural channels; and it wastes a part of it in the expenses of administration. Could we do without taxes altogether, we should all be better

off. But we cannot; and since taxes we must have, we must have also a system of financial administration. We should be better without one, but we have got to have it. Since we have got to have it, it is a good thing to understand how it works and to keep a close watch upon it to see that it works well: for it is rather an elaborate engine, and very apt to leak.

# APPENDIX A

BELOW will be found (*a*) a Vote from the Estimates, on which are based the year's account-keeping and financial business in respect of the services included, and (*b*) the Appropriation Account in respect of that Vote, which closes them. The National Portrait Gallery Vote, which is Vote 4 of Class IV. of the Civil Service Estimates, has been chosen as a simple one which shows well the outlines of the system. The extracts have been abbreviated.

(*a*) ESTIMATES, CIVIL SERVICES, 1922–23: CLASS IV. (4) NATIONAL PORTRAIT GALLERY.

(i.) Estimate of the Amount required in the Year ending 31st March, 1923, to defray the Salaries and Expenses of the National Portrait Gallery, including a Grant in Aid for the purchase of Portraits.

Eight Thousand Five Hundred and Nine Pounds.

(ii.) Sub-heads under which this Vote will be accounted for by the Trustees of the National Portrait Gallery.

| — | 1922–23. | 1921–22. | Increase. | Decrease. |
|---|---|---|---|---|
| | £ | £ | £ | £ |
| A.—Salaries, Wages, and Allowances | 6,304 | 7,366 | — | 1,062 |
| B.—Purchase of Portraits (Grant in Aid) [1] | 1,063 | 1,033 | 30 | — |
| C.—Warders | 1,270 | 1,734 | — | 464 |
| D.—Incidental Expenses | 650 | 1,100 | — | 450 |
| E.—Uniforms | 107 | 326 | — | 219 |
| Gross Total . . £ | 9,394 | 11,559 | 30 | 2,195 |
| Deduct: | | | | |
| F.—Appropriations in Aid | 885 | 715 | — | 170 |
| Net Total . . £ | 8,509 | 10,844 | 30 | 2,365 |

Net Decrease . £2,335

[1] The expenditure out of the Grant in Aid will be subject to audit by the Comptroller and Auditor General, but the unexpended balance (if any) of the sums issued will not be surrendered at the close of the financial year.

(iii.) Details of the foregoing.

A.—Salaries, Wages, and Allowances: (a)

| Numbers. | | | 1922–23. | 1921–22. |
|---|---|---|---|---|
| 1921–22. | 1922–23. | | | |
| | | | £ | £ |
| 1 | 1 | Director, Keeper, and Secretary . . . . . (£900) | 900 | 900 |
| 1 | 1 | Clerk . (£200–£10–£300) | 229 | 219 |
| 1 | 1 | Clerk . . (£60–£250) | 85 | 60 |
| 1 | 1 | Typist, Temporary (inclusive) | 133 | 120 |

[Here follow details of the other salaries, etc. borne on the Vote.]

| | | | | |
|---|---|---|---|---|
| | | Bonus . . . . . . | 2,546 | 3,584 |
| 34 | 32 | Total for Salaries, etc.. . | 6,304 | 7,366 |

B.—Purchase of Portraits (Grant in Aid):

| | | |
|---|---|---|
| Normal grant . . . . . . | 750 | 750 |
| Equivalent of amount derived from the sale of certain photographs and paid into Subhead F. Appropriations in Aid, in 1921–22 . . . . . . . | 313 | 283 |
| Total for Purchase of Portraits .£ | 1,063 | 1,033 |

C.—Warders:

[Details of salaries of Warders.]

D.—Incidental Expenses:

| | | |
|---|---|---|
| Cost of catalogues and picture postcards . | 150 | 400 |
| Cleaning pictures and busts; glazing, moving, and hanging pictures; cost of frames, gallery requisites, and descriptive tablets; purchase of prints and photographs; travelling and office expenses, etc. | 500 | 700 |
| Total for Incidental Expenses . .£ | 650 | 1,100 |

E.—Uniforms:

| | | |
|---|---|---|
| For the attendant staff when on duty in the Gallery; to be supplied by the Controller, Post Office Stores Department . .£ | 107 | 326 |

F.—Appropriations in Aid:

| | 1922–23. | 1921–22. |
|---|---|---|
| | £ | £ |
| Admission Fees (formerly paid over to the Exchequer as extra receipts) | 250 | 315 |
| Proceeds of sale of catalogues, photographs, and picture postcards | 635 | 400 |
| Total for Appropriations in Aid . £ | 885 | 715 |

(b) Appropriation Account, 1922–23: Class IV. (4).
Vote for National Portrait Gallery.

Account of the Sum Expended, in the Year ended 31st March, 1923, compared with the Sum Granted, for the Salaries and Expenses of the National Portrait Gallery, including a Grant in Aid for the Purchase of Portraits.

| Service. | Grant. | Expenditure. | Expenditure compared with Grant. Less than Granted. | More than Granted. |
|---|---|---|---|---|
| | £ | £ s. d. | £ s. d. | £ s. d. |
| A.—Salaries, Wages, and Allowances. | 6,304 | 5,984 4 6 | 319 15 6 | — |
| B.—Purchase of Portraits (Grant in Aid) | 1,063 | 1,063 0 0 | — | — |
| C.—Warders | 1,270 | 1,224 4 5 | 45 15 7 | — |
| D.—Incidental Expenses | 650 | 585 15 3 | 64 4 9 | — |
| E.—Uniforms | 107 | 74 10 9 | 32 9 3 | — |
| Gross Total . £ | 9,304 | 8,931 14 11 | 462 5 1 | — |
| | | | Surplus of Gross Estimate over Expenditure, £462 5s. 1d. Surplus of Appropriations in Aid realised, £215 0s. 10d. Total Surplus to be surrendered, £677 5s. 11d. | |
| F.—Appropriations in Aid | Estimated 885 | Realized 1,100 0 10 | | |
| Net Total . £ | 8,509 | 7,831 14 1 | | |

Explanation of the Causes of Variation between Expenditure and Grant.

A.—Savings were effected through the fall in the bonus (£170) and by suppressing one post on the Attendant Staff (£150).

C.—Due to a reduction in bonus.

D.—The sum expended on postcards and other reproductions was less by £20 than that provided, and a saving was made on the cost of frames glazing, etc. (£44).

E.—Due to unfilled vacancies on the staff and the fall in the cost of uniforms.

F.—Receipts from all sources were greater than estimated: admission fees were charged on two extra week-days from 1st November, 1922, and the improved sale of publications was due to the increase in the number of visitors.

Extra Remuneration (exceeding £50).

The Director (£900) received in fees from the Inland Revenue the sum of £230 15*s.* for inspections and reports.

10th October, 1923. *James D. Milner,*
Accounting Officer.

GRANT IN AID ACCOUNT.

| | £ s. d. | | £ s. d. |
|---|---|---|---|
| Balance on 1st April, 1922 . . . | 2,652 18 6 | Portraits purchased during the year . | 1,082 18 0 |
| Grant in Aid, 1922–23 . . . | 1,063 0 0 | Balance on 31st March, 1923 . . . | 2,633 0 6 |
| | £3,715 18 6 | | £3,715 18 6 |

10th October, 1923. *James D. Milner,*
Accounting Officer.

I have examined the foregoing Accounts in accordance with the provisions of the Exchequer and Audit Departments Act, 1921. I have obtained all the information and explanations that I have required, and I certify, as the result of my audit, that in my opinion these Accounts are correct.

*Malcolm G. Ramsay,*
Comptroller and Auditor General.

# APPENDIX B

## GENERAL ABSTRACT OF ARMY ESTIMATES, 1923–24.

| Page. | — | 1923–24. Gross Estimate. | 1923–24. Sums Receivable. | 1923–24. Net Estimate. | 1922–23. Gross Estimate. | 1922–23. Sums Receivable. | 1922–23. Net Estimate. | Increase on Net Estimates. | Decrease on Net Estimates. |
|---|---|---|---|---|---|---|---|---|---|
| | NUMBERS. | | | Total Numbers. | | | Total Numbers. | Numbers. | Numbers. |
| 7 | Vote A.—Number of Men on the Establishment of the Army, exclusive of those serving in India | — | — | 170,800 | — | — | 215,000 | — | 44,200 |
| | HEADS OF COST. | £ | £ | £ | £ | £ | £ | £ | £ |
| 22 | Head I.—Maintenance of Standing Army | 28,361,600 | 229,600 | 28,132,000 | 35,603.700 | 252,400 | 35,351,300 | — | 7,219,300 |
| 34 | Head II.—Territorial Army and Reserve Forces | 7,220,100 | 20,100 | 7,200,000 | 8,103,200 | 20,200 | 8,083,000 | — | 883,000 |
| 39 | Head III.—Educational, etc., Establishments, and Working Expenses of Hospitals, Depôts, etc. | 8,081,200 | 665,200 | 7,416,000 | 9,951,800 | 740,800 | 9,211,000 | — | 1,795,000 |
| 161 | Head IV.—War Office, Staff of Commands, etc. | 2,697,250 | 6,250 | 2,691,000 | 3,361,200 | 5,700 | 3,355,500 | — | 664,500 |
| 172 | Head V.—Capital Accounts | Cr. *292,250* | 1,583,750 | Cr. *1,876,000* | Cr. *497,900* | 2,133,700 | Cr. *2,631,600* | 755,600 | — |
| 196 | Head VI.—Terminal and Miscellaneous Charges and Receipts | 6,914,100 | 4,932,100 | 1,982,000 | 13,000,500 | 6,181,400 | 6,819,100 | — | 4,837,100 |
| 204 | Head VII.—Half Pay, Retired Pay, Pensions, and Civil Superannuation | 8,649,500 | 1,131,500 | 7,518,000 | 9,729,000 | 1,111,800 | 8,617,200 | — | 1,099,200 |
| | Total | 61,631,500 | 8,568,500 | 53,063,000 | 79,251,500 | 10,446,000 | 68,805,500 | — | 15,742,500 |
| 6 | Repayment by the Colonial Office for expenditure in the Middle East | | 553,000 | Cr. *553,000* | | 4,930,000 | Cr. *4,930,000* | 4,377,000 | — |
| | Total | 61,631,500 | 9,121,500 | 52,510,000 | 79,251,500 | 15,376,000 | 63,875,500 | — | 11,365,500 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **Add:** | | | | | | | | |
| Decrease of amounts due by War Department at end of financial year as compared with beginning . . . . . . . | 661,500 | | 582,000 | 295,500 | | *Cr.* *5,500* | 587,500 | — |
| Decrease of amounts due to War Department at end of financial year as compared with beginning . . . . . . . | | 79,500 | | | 301,000 | | | |
| | | | 53,092,000 | | | 63,870,000 | | |
| **Less:** | | | | | | | | |
| Items of cost for which no cash payment will be made (*See* Appendix IX.) . . . . | 1,093,000 | 1,000 | *Cr.* *1,092,000* | 1,570,000 | | *Cr.* 1,570,000 | 478,000 | — |
| Estimated Cash required for Army Services . . . . . . | | | 52,000,000 | | | 62,300,000 | — | 10,300,000 |

## CASH STATEMENT, 1923–24.

| | 1923–24. | 1922–23. |
|---|---|---|
| **Estimated** | | |
| Cash payments chargeable to Army Funds . | £ 61,200,000 | £ 77,977,000[1] |
| **Less:** Receipts (Appropriations in Aid) . | 9,200,000 | 15,677,000 |
| Cash required for Army Services . . . £ | 52,000,000 | 62,300,000[1] |

Derby. Cavan, C.I.G.S. H. J. Creedy.
Walter Guinness. R. Whigham, A.G. C. Harris.
F. Stanley Jackson. Travers Clarke, Q.M.G.
J. P. Du Cane, M.G.O.

War, Office,
3rd March, 1923.

[1] Excludes the Supplementary Estimate of 1st December, 1922, for £340,000 on account of compensation to Army Officers and others in connection with the failure of Messrs. Sir C. R. McGrigor, Bart., & Co.

# APPENDIX C

An Instructive Summary of the Appropriation Account in the following
This Summary, for 1920–21, shows practical examples of many

GENERAL ABSTRACT OF APPRO-

(After Audit by the Comptroller and Auditor General, and Review

| SERVICE. | Grants and Estimated Receipts, 1920–21. | | |
|---|---|---|---|
| | Estimated Gross Expenditure. (1.) | Estimated Receipts in Aid of Grants. (2.) | Exchequer Grants. (3.) |
| | £ | £ | £ |
| Navy | 105,283,281 | 14,410,981 | 90,872,300 |
| Army | 205,000,000 | 40,250,000 | 164,750,000 |
| Army (Ordnance Factories) | 6,878,100 | 6,878,000 | 100 |
| Air Services | 25,202,319 | 2,210,089 | 22,992,230 |
| Total, Naval, Military, and Air Services £ | 342,363,700 | 63,749,070 | 278,614,630 |
| Civil Services: | | | |
| Class I. | 14,638,443 | 1,153,796 | 13,484,647 |
| „ II. | 25,460,273 | 3,446,442 | 22,013,831 |
| „ III. | 20,710,287 | 915,298 | 19,794,989 |
| „ IV. | 59,949,548 | 118,940 | 59,830,608 |
| „ V. | 5,657,047 | 415,110 | 5,241,937 |
| „ VI. | 5,217,602 | 14,800 | 5,202,802 |
| „ VII. | 98,780,969 | 9,595,960 | 89,185,009 |
| Unclassified Services | 376,288,257 | 47,196,700 | 329,091,557 |
| Total Civil Services . £ | 606,702,426 | 62,857,046 | 543,845,380 |
| Revenue Departments: | | | |
| Customs and Excise | 4,868,771 | 184,400 | 4,684,371 |
| Inland Revenue | 6,674,080 | 10,000 | 6,664,080 |
| Post Office | 54,989,371 | 1,001,249 | 53,988,122 |
| Total, Revenue Departments . £ | 66,532,222 | 1,195,649 | 65,336,573 |
| | 1,015,598,348 | 127,801,765 | 887,796,583 |
| Deduct—Expenditure from Votes for War Bonus and Civil Service Assimilation already included under other Votes. (See Column 8.) | — | — | — |
| Total for Voted Services . £ | 1,015,598,348 | 127,801,765 | 887,796,583 |

Consolidated Fund:

National Debt Services { (a) Inside Fixed Debt Charge
(b) Outside Fixed Debt Charge

Road Fund (including Road Improvement Fund)

Payments to Local Taxation Accounts, etc.

Land Settlement

Other Consolidated Fund Services

Total of Consolidated Fund Services

Grand Total of

[1] The Gross Expenditure in excess of the Estimate for Army was met by Aid to the Amount of £5,258,343 11*s*. 6*d*.

# (APPROPRIATION ACCOUNTS)

form is appended to the Report of the Committee of Public Accounts.
of the arrangements discussed in the foregoing pages.

PRIATION ACCOUNTS. 1920–1921.

by the Public Accounts Committee of the House of Commons).

| Expenditure, 1920–1921. | | | Differences between Exchequer Grants and Net Expenditure. (Columns 3 and 6.) | |
|---|---|---|---|---|
| Gross Expenditure. | Actual Receipts in Aid. | Net Expenditure. | Surpluses. | Deficits. |
| (4.) | (5.) | (6.) | (7.) | (8.) |
| £ | £ | £ | £ | £ |
| 112,793,808 | 20,288,518 | 92,505,290 | — | 1,632,990 |
| [1] 210,258,443 | 45,580,894 | 164,677,549 | 72,450 | — |
| 6,567,025 | 5,526,752 | 1,040,272 | — | 1,040,172 |
| 23,949,369 | 3,250,101 | 20,699,268 | 2,292,961 | — |
| 353,568,647 | 74,646,267 | 278,922,380 | 2,365,412 | 2,673,162 |
| 13,607,562 | 1,395,995 | 12,211,567 | 1,347,710 | 74,630 |
| 22,846,131 | 3,599,193 | 19,246,938 | 3,168,864 | 401,972 |
| 20,990,842 | 1,087,246 | 19,903,596 | 502,814 | 611,421 |
| 59,355,525 | 124,309 | 59,231,215 | 648,041 | 48,648 |
| 5,394,519 | 701,377 | 4,693,141 | 548,795 | — |
| 3,889,349 | 15,525 | 3,873,823 | 1,402,581 | 73,602 |
| 78,194,106 | 3,919,542 | 74,274,563 | 14,951,233 | 40,788 |
| 329,412,237 | 63,328,079 | 266,084,158 | 63,036,303 | 28,904 |
| 533,690,274 | 74,171,270 | 459,519,004 | 85,606,344 | 1,279,968 |
| 5,526,142 | 251,504 | 5,274,637 | [2] 67,104 | 657,371 |
| 7,214,505 | 29,273 | 7,185,231 | [2] 19,273 | 540,425 |
| 63,215,746 | 1,189,795 | 62,025,951 | [2] 188,546 | 8,226,375 |
| 75,956,393 | 1,470,573 | 74,485,820 | 274,924 | 9,424,171 |
| 963,215,315 | 150,288,111 | 812,927,204 | 88,246,681 | 13,377,303 |
| 10,702,940 | — | 10,702,940 | — | 10,702,940 |
| 952,512,375 | 150,288,111 | 802,224,263 | 88,246,681 | 2,674,362 |
| | Estimated Expenditure. | Actual Expenditure. | Less than Estimate. | More than Estimate. |
| . . . . | 24,500,000 | 24,500,000 | — | — |
| . . . . | 320,500,000 | 325,098,615 | — | 4,598,615 |
| . . . . | 6,650,000 | 8,936,689 | — | 2,286,689 |
| . . . . | 10,818,000 | 10,785,503 | 32,496 | — |
| . . . . | 12,000,000 | 6,929,793 | 5,070,207 | — |
| . . . . | 1,730,000 | 1,796,275 | — | 66,275 |
| . . . £ | 376,198,000 | 378,046,876 | 5,102,703 | 6,951,580 |
| Expenditure . . £ | | 1,180,274,140 | | |

a nominal Excess Vote of £100, taken in March, 1922, and by Appropriations in

[2] Surplus of Receipts in Aid over Estimate.

# APPENDIX D

The following is a list of the principal Accounts, Returns, and papers relating to national finance which are published annually and are of general interest. Together they tell the taxpayer all that he needs to know about the state of the nation's purse.

(*a*) Finance Accounts of the United Kingdom for the year.

A summary of the year's finance, giving an account of Receipts and issues out of the Exchequer Account for the year, and statements showing the position of the National Debt.

(*b*) Estimates.

There are five bulky volumes, one each for the Civil Service, Revenue Departments, Navy, Army, and Air Force.

(*c*) Appropriation Accounts.

There are four volumes, one each for the Civil Service and Revenue Departments, Navy, Army, and Air-Force.

(*d*) Returns relating to Revenue and Expenditure.

1. Financial Statement of Revenue and Expenditure made by the Chancellor of the Exchequer when opening the Budget. This is a Parliamentary Paper published annually after the Budget speech.

2. Memorandum on Present and Pre-war Expenditure.

An analysis, published each year, of the gross expenditure, classified under forty broad headings, in each year since 1913–14.

3. Public Social Services Return.

The total expenditure, including expenditure financed from rates, on some of the principal forms of public social service.

(*e*) Returns relating to Debt.

1. Return as to the National Debt. This annual Command Paper gives tables showing the state of the debt since 1913–14.[1] A series of notes at the end make a valuable summary of the history of all the chief operations in connection with the debt.

2. An annual Parliamentary Return relating to the National

[1] The 1915 Return gives complete figures from 1836 to 1915.

Debt: this gives tables showing the Dead Weight Debt and other Capital Liabilities since 1875.

3. Return as to Sinking Funds: this shows each sum received by the National Debt Commissioners on account of the Sinking Funds and gives details of each purchase of stock and cash made on account of them.

(*f*) Accounts of Funds: these are annual Parliamentary Papers. Of most general interest are those of the—

1. Local Loans Fund.
2. Civil Contingencies Fund.
3. Treasury Chest Fund.
4. Development Fund.
5. Post Office Savings Bank.

(*g*) Reports of Various Bodies.

1. Reports of the Committee of Public Accounts. Two or more reports are represented yearly, which are finally printed together as a Blue Book.

The Exchequer and Audit Department publishes a volume of the greatest value, "Epitome of the Reports from the Committee of Public Accounts, 1857–1910," which is brought up to date from time to time. This is an illuminating manual of "case law," as it were, and of principles and precedents, affecting many of the most important questions of public finance.

2. Report of the Select Committee on the Estimates.

3. Reports of the Commissioners of Inland Revenue, and of Customs and Excise. These Blue Books contain the fullest details as to the annual revenue.

In addition to these, the Annual Statistical Abstract of the United Kingdom contains several valuable comparative and historical tables of revenue, expenditure, and debt, in a summary form.

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